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# ADOPTING A JURISDICTIONAL APPROACH TO THE RIGHTS OF ASSET PURCHASERS FROM THE FDIC

Nicole Sabado

## INTRODUCTION

The Federal Deposit Insurance Corporation ("FDIC") insures deposits<sup>1</sup> of the national and state banks and thrifts that are its member institutions. In the event of a bank failure,<sup>2</sup> the FDIC provides insurance coverage to depositors in these institutions up to the amount of \$100,000 per depositor.<sup>3</sup> When the FDIC carries out its role as an insurer and takes control of a failed or failing<sup>4</sup> bank, the FDIC must preserve the confidence of the individual depositor and the confidence of the nation in the banking system.<sup>5</sup> While depositors' funds are protected by this insurance fund, it is the full faith and credit of the United States government, and ultimately of the American taxpayers, that stand behind the FDIC insurance fund.<sup>6</sup>

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1. See 12 U.S.C. § 1811 (1994). Thrifts refer to the following institutions: savings and loans, buildings and loans, and savings banks. See Peter P. Swire, *Bank Insolvency Law Now That It Matters Again*, 42 Duke L.J. 469, 473 n.7 (1992). Since 1989, bank and thrift regulation have been treated essentially the same. See *id.*

2. "Simply put, a bank fails when its liabilities exceed the value of its assets." Managing the Crisis: The FDIC and RTC Experience 43 (FDIC 1998) [hereinafter *Managing the Crisis*].

3. See 12 U.S.C. § 1821(a)(1)(B).

4. "[A]s a matter of law, a troubled institution is one that has not yet failed but is in danger of doing so if current trends in its financial condition continue." Michael P. Malloy, III *Banking Law & Regulation* § 11.1, at 11.1-11.2 (1994).

5. See *Managing the Crisis*, *supra* note 2, at 8. As an insurer of the deposits of the nation's banks and thrifts the FDIC faces the following challenges:

In the event of institution failures, the FDIC maintains stability and public confidence in the system by providing the public with ready access to their insured funds. The FDIC helps ensure the stability of the financial system in times of stress by providing timely or quick resolution of failed institutions. This stability helps promote public confidence in the system and restores liquidity to the economy.

*Id.* at 7-8.

6. See Fred Galves, *Might Does Not Make Right: The Call for Reform of the Federal Government's D'Oench, Duhme and 12 U.S.C. § 1823(e) Superpowers in Failed Bank Litigation*, 80 Minn. L. Rev. 1323, 1333-34 (1996) [hereinafter *Galves, Might Does Not Make Right*]; James J. Boteler, Comment, *Protecting the American Taxpayers: Assigning the FDIC's Six Year Statute of Limitations to Third Party Purchasers*, 24 Tex. Tech. L. Rev. 1169, 1169 (1993); see also Malloy, *supra* note 4, §

A financial crisis in the banking industry in the 1980s and 1990s presented great challenges to the FDIC in its role as an insurer.<sup>7</sup> In response to the crisis, Congress enacted comprehensive legislation called the Financial Institutions Reform, Recovery and Enforcement Act of 1989<sup>8</sup> ("FIRREA") to bolster the FDIC's ability to manage the billions of dollars in assets of failed and failing banks that fell under the FDIC's control.<sup>9</sup> Courts also expanded the FDIC's common law powers during the crisis to aid the FDIC in its litigation efforts to recover upon these assets.<sup>10</sup>

Courts have analyzed the status of federal subject matter jurisdiction in actions when the FDIC sells assets once held by a failed bank to a private party and then leaves the litigation.<sup>11</sup> The circuits are split as to whether federal subject matter jurisdiction exists under 12 U.S.C. § 1819(b)(2)(A) when the FDIC has withdrawn from an ongoing litigation by the assignment of its rights to a private party. This Note explores the issues related to federal court jurisprudence raised by this split in authority.

Part I provides background on the FDIC and describes the agency's role when an insured depository institution such as a bank or thrift becomes financially troubled.<sup>12</sup> This part examines the FDIC's statutory and common law powers that allow the agency to meet its obligations to the depositors of these insured banks and thrifts.<sup>13</sup> Part II discusses the constitutional dimension of the subject matter jurisdiction of federal courts. Other concerns pertinent to federal jurisdiction are introduced, including federalism and prudential concerns such as efficiency and fairness.<sup>14</sup> Part II also analyzes § 1819(b)(2)(A), the FDIC's statutory grant of federal jurisdiction. Part III discusses the decisions of the circuit courts of appeals that created the legal controversy. This part outlines the distinct approaches of the minority and majority circuits regarding whether FIRREA allows a private party that buys assets of a failed bank or thrift from the FDIC to receive the benefit of the FDIC's federal court jurisdiction. Relying on federal common law, the majority holds that these private

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11.3.2, at 11.21 ("The ultimate liability of the federal government in a situation involving a failed depository institution is the obligation for insured deposits of the institution.").

7. See *Managing the Crisis*, *supra* note 2, at 6.

8. Pub. L. No. 101-73, 103 Stat. 183 (1989) (codified as amended in scattered sections of 2, 12 and 42 U.S.C.).

9. See *Managing the Crisis*, *supra* note 2, at 6. Two thousand nine hundred and twelve (2,912) federally insured depository institutions failed between 1980-1994. See *id.* at 4. They held a combined total of \$924 billion dollars in assets. See *id.*

10. See, e.g., Galves, *Might Does Not Make Right*, *supra* note 6, at 1349 (noting that expansion of the FDIC's common law "accelerated" in the 1980s).

11. See discussion *infra* Part III.

12. See discussion *infra* Part I.A.

13. See discussion *infra* Parts I.A.-B.

14. See discussion *infra* Parts II.B.-C.

parties are assignees of the FDIC and thus inherit the FDIC's federal jurisdiction under FIRREA.<sup>15</sup> Alternatively, these courts apply the time-of-filing rule to hold that no jurisdictional defect was created.<sup>16</sup> The minority argues that a plain meaning analysis of FIRREA supports the opposite conclusion; Congress did not extend its grant of federal jurisdiction to assignees of the FDIC.<sup>17</sup>

Part IV outlines three approaches to the legal controversy based in federal court jurisprudence and suggests that the proper approach to the legal controversy must include analysis from a jurisdictional standpoint. First, this part considers whether it is possible to assign federal subject matter jurisdiction when it is based upon a party's federal agency status.<sup>18</sup> Second, this part explores the application and the policy of the time-of-filing rule as a method of resolving the conflict.<sup>19</sup> The third approach presents the question of whether courts may properly apply the supplemental jurisdiction statute to decide if a court may exercise jurisdiction over the non-diverse, remaining parties after the FDIC has exited the ongoing litigation and only state law is at issue.<sup>20</sup> In Part V the Note evaluates the merits of all these approaches. It concludes that Congress should amend FIRREA to include a grant of federal jurisdiction to these FDIC assignees.

## I. THE FDIC

The FDIC supervises troubled depository institutions<sup>21</sup> and has the power to declare that an institution is in default.<sup>22</sup> When dealing with these institutions, the FDIC acts in its corporate capacity as an insurer and as a conservator or receiver of the bank or thrift.<sup>23</sup> As a conservator, the FDIC assumes the day-to-day operations of a financial institution.<sup>24</sup> In contrast, when the FDIC acts as a receiver, it steps into the shoes of the bank in default and acts as a trustee.<sup>25</sup> It becomes a successor to all rights, titles and powers of the depository

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15. See discussion *infra* Part III.A.1.

16. See discussion *infra* Part III.A.2.

17. See *infra* notes 211-25 and accompanying text.

18. See discussion *infra* Part IV.A.

19. See discussion *infra* Part IV.B.

20. See discussion *infra* Part IV.C.

21. See 12 U.S.C. § 1821(c)(4), (6), (9)-(10), (13) (1994).

22. See *id.* § 1821(c)(4)(A). "[A]s a matter of law a depository institution is failing only if it has been declared to be so by its primary regulator." Malloy, *supra* note 4, § 11.1, at 11.2.

23. See 12 U.S.C. § 1821(c), (e) (requiring the FDIC to accept appointment as receiver of a failed bank); see also Malloy, *supra* note 4, § 11.3.2, at 11.24-11.29 (describing supervision of troubled depository institutions).

24. See Financial Institutions Reform Act of 1989 Conference Report ¶ 4208 in Financial Institutions Reform, Recovery and Enforcement Act of 1989: P.L. 101-73, 103 Stat. 183, as signed by the President on August 9, 1989.

25. See *id.*; Galves, *Might Does Not Make Right*, *supra* note 6, at 1340-41.

institution and may even liquidate the institution's assets.<sup>26</sup> In its corporate capacity, the FDIC is responsible for "guaranteeing the timely funding of insured deposits."<sup>27</sup> To do so, the FDIC must either pay the depositor's insured claims or "[make] available to each depositor a transferred deposit in a new insured depository institution in the same community or in another insured depository institution in an amount equal to the insured deposit."<sup>28</sup>

### A. Managing Bank Failure

When dealing with either a troubled or a defaulted institution, the FDIC must pursue a course of action that is both of minimal cost to the deposit insurance fund and best preserves the value of assets owed to creditors.<sup>29</sup> At the same time, the FDIC must minimize disruptions to bank depositors, such as "avoiding returned checks, lost time value of money, and loss of confidence associated with the alternative of closing the failed bank."<sup>30</sup> When a troubled institution is not yet in default, the FDIC must act to avoid the worst possible consequence of such disruptions, a "bank run," a situation in which depositors withdraw their accounts from institutions in financial distress and cause them to become insolvent.<sup>31</sup>

As an alternative to liquidating assets to pay off deposits, the FDIC frequently engages in a purchase and assumption transaction ("P&A") with an acquirer bank to deal with a failing financial institution.<sup>32</sup> P&As have been called the "favored resolution policy of the FDIC,"<sup>33</sup> and the FDIC entered into P&As to manage 73.5% of the 1,617 failed and failing banks during the time period of 1980 to 1994.<sup>34</sup> For the FDIC, a P&A is beneficial because it requires less of a cash outlay from the insurance fund than would be needed to pay off all insured depositors' claims.<sup>35</sup> The acquirer bank expands its

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26. See 12 U.S.C. § 1821(d)(2)(A)-(C), (E).

27. Managing the Crisis, *supra* note 2, at 6.

28. 12 U.S.C. § 1821(f)(1).

29. See *id.* § 1823(c)(4)(A)(ii) (requiring least cost resolution); § 1823(d)(3)(D) (requiring that sale or disposition of assets by FDIC "maximizes the net present value return" and "minimizes the amount of any loss realized in the resolution of cases"); § 1821(d)(13)(E) (same, when the FDIC acts as conservator or receiver); Marie T. Reilly, *The FDIC as Holder in Due Course: Some Law and Economics*, 1992 Colum. Bus. L. Rev. 165, 173.

30. Reilly, *supra* note 29, at 175.

31. See Galves, *Might Does Not Make Right*, *supra* note 6, at 1339.

32. See 12 U.S.C. § 1823(c); see generally *Gunter v. Hutcheson*, 674 F.2d 862, 865 (11th Cir. 1982) (describing a P&A).

33. Managing the Crisis, *supra* note 2, at 14. The term resolution refers to "a disposition plan for a failed or failing institution." *Id.* at 3 n.1.

34. See *id.* at 14.

35. See Reilly, *supra* note 29, at 175.

business at low risk and depositors avoid the uncertainty of the closing and liquidation of a failed bank.<sup>36</sup>

A P&A has characteristics of a merger<sup>37</sup> and it also combines elements of reorganization and liquidation.<sup>38</sup> In a P&A, an acquirer bank purchases the assets<sup>39</sup> and assumes the liabilities<sup>40</sup> of a failed bank. The transaction is usually accomplished overnight in order to preserve the going concern value<sup>41</sup> of the failed bank.<sup>42</sup> Thus, a P&A avoids any inconvenience to depositors related to a disruption in banking services.<sup>43</sup> The FDIC first places the bank into receivership and sells the "bad"<sup>44</sup> assets to the FDIC acting in its corporate capacity.<sup>45</sup> The FDIC then sells the assets of highest banking quality to the acquirer bank.<sup>46</sup> As a result, liabilities assumed by the acquirer bank exceed the purchased assets.<sup>47</sup> The FDIC then pays the acquirer a premium to make up for the shortfall between the value of the liabilities the acquirer assumed and the assets the acquirer purchased.<sup>48</sup>

### B. Congressional Response to Commercial Bank and S&L Crises

During the 1980s, the widespread failure of commercial banks and the collapse of nationwide savings and loans ("S&L") brought great public scrutiny to the insurance fund.<sup>49</sup> Between 1980 and 1994, 1,617

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36. See *Gunter*, 674 F.2d at 865.

37. See Malloy, *supra* note 4, § 11.32, at 11.27.

38. See Warren L. Dennis & John R. Simon, *Litigation with the FDIC and the RTC: The Evolving D'Oench Doctrine Superpower Defense*, 47 Bus. Law. 1319, 1320 (1992).

39. A bank's loan portfolio is its primary asset. See Reilly, *supra* note 29, at 166. The portfolio is a bank's rights to receive repayment from borrowers. See *id.*

40. A bank's liabilities are its deposits. See Malloy, *supra* note 4, § 11.3.2, at 11.24.

41. Going concern value refers to "the value of the assets of a business as an operating, active concern, rather than merely as items of property (book value of assets alone) which would be the case in a liquidation sale. Such value includes goodwill." Black's Law Dictionary 691 (6th ed. 1990). When a business is purchased, goodwill is a term that is used to reflect attributes such as "the value of good customer relations, high employee morale, a well respected business name, etc. which are expected to result in greater than normal earning power." *Id.* at 694.

42. See *Gunter v. Hutcheson*, 674 F.2d 862, 865 (11th Cir. 1982).

43. See *id.*

44. In early P&A transactions, acquirer banks only purchased assets of cash and cash equivalents and the FDIC retained loans, the assets with risk. See *Managing the Crisis*, *supra* note 2, at 15. Later, the FDIC used a put option in their contract with acquirer banks. See *id.* With a put option, the acquirer had the opportunity during a specific timeframe to return to the FDIC those assets that they did not wish to keep. See *id.* As a result, "acquirers were able to 'cherry pick' the assets, choosing to keep only those with market values above book value or assets having little risk, while returning all other assets." *Id.*

45. See *Gunter*, 674 F.2d at 865.

46. See *id.*

47. See *id.*

48. See *id.*

49. A confluence of factors caused the thrift industry to fail, including, "(i) poorly

national banks closed or received FDIC financial assistance.<sup>50</sup> During the same period of time, 1,295 S&Ls closed or received financial assistance from the Federal Savings and Loan Insurance Corporation.<sup>51</sup> The bailout of the S&L industry totaled around \$145 billion and has been called "[t]he greatest transfer of wealth outside armed rebellion in the history of this country."<sup>52</sup> The S&L crisis also came at huge taxpayer expense, with some cost estimates totaling \$1 trillion over the next several decades.<sup>53</sup>

In 1989, Congress passed FIRREA<sup>54</sup> to create a comprehensive statutory regime for the FDIC to address the crisis in the banking industry.<sup>55</sup> In FIRREA, Congress dissolved the Federal Savings and Loan Insurance Corporation and created the Resolution Trust Corporation, an interim agency, to manage failed savings associations.<sup>56</sup> Congress strengthened the enforcement powers of federal regulators of depository institutions and increased civil sanctions and criminal penalties for defrauding depository institutions and their depositors.<sup>57</sup>

As a receiver and as an insurer, much FDIC litigation involved collecting upon unacceptable assets that the FDIC acquired from P&A transactions.<sup>58</sup> These assets were usually "in bulk, under distress

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timed industry-wide deregulation; (ii) the rising interest rate environment of the late 1970s and early 1980s; (iii) poor internal management in the thrift industry; (iv) a lack of adequate government supervision and regulation; (v) a regional economic collapse, specifically in the Southwest; and (vi) insider trading and fraud." Anthony C. Providenti, Jr., *Playing with FIRREA, Not Getting Burned: Statutory Overview of the Financial Institutions Reform, Recovery and Enforcement Act of 1989*, 59 Fordham L. Rev. 323, 324 (1991).

50. See *Managing the Crisis*, *supra* note 2, at 4.

51. See *id.*

52. Michael Keeley & Toni Scott Reed, "Superpowers" of Federal Regulators: *How the Banking Crisis Created an Entire Generation of Bond Litigation*, 31 Tort & Ins. L.J. 817, 825 (1996).

53. See Galves, *Might Does Not Make Right*, *supra* note 6, at 1335 n.51.

54. When enacted, FIRREA was the "largest piece of federal legislation affecting the U.S. banking and financial industry since 1933." Boteler, *supra* note 6, at 1171 n.22.

55. See Swire, *supra* note 1, at 473-74.

56. See Deirdre M. Roarty, Note, *Resolving Pre-Receivership Claims Against Failed Savings and Loans: An Unnecessarily Exhausting Experience*, 63 Fordham L. Rev. 2315, 2321 (1995). The RTC was under the general supervision of the FDIC. See *id.* Under 12 U.S.C. § 1441a(b)(3)(c) of FIRREA, the RTC exercised the powers available to the FDIC under the Federal Deposit Insurance Act. See *id.* at 2322. Because it was a temporary agency, the RTC went into sunset on July 1, 1995, and any savings and loan association in receivership at that time was assumed by the FDIC. See *id.* at 2321-22. "During its lifetime the RTC closed or merged 747 thrifts, protected 25 million depositor accounts and sold more than \$465 billion in assets, including 120,000 real estate properties." See Keeley & Reed, *supra* note 52, at 824. The FDIC is now the agency appointed as receiver of all depository institutions. See Roarty, *supra*, at 2322. When this Note refers to the RTC, the conclusions are applicable to lawsuits involving the FDIC.

57. See Boteler, *supra* note 6, at 1172.

58. See *id.* at 1172-73 (discussing the FDIC litigation powers and the financial

conditions, and . . . non-performing or otherwise objectionable to a healthy bank."<sup>59</sup> Congress gave the FDIC a repertoire of litigation powers to aid in the collection of these assets, including the ability to avoid punitive damages, stay judicial proceedings, and remove pending cases from state to federal court.<sup>60</sup> FIRREA also gave the FDIC the benefit of the six-year federal statute of limitations.<sup>61</sup> These statutory protections, along with FDIC common law powers, are often called "superpowers."<sup>62</sup> They all serve to advance the policy of safeguarding the deposit insurance fund against depletion.<sup>63</sup>

### C. Federal Common Law Powers – D'Oench, Duhme

The FDIC benefited not only from enhanced statutory powers, but also from the expansive interpretation that courts gave to the FDIC's common law powers during the financial crises of the commercial banking and S&L industry. In *D'Oench, Duhme & Co. v. FDIC*,<sup>64</sup> the Supreme Court created a federal common law rule of estoppel that allowed the FDIC to void defenses asserted by debtors that were based on unrecorded side agreements.<sup>65</sup> The *D'Oench, Duhme* doctrine ("*D'Oench, Duhme*") and related common law powers<sup>66</sup> allow the FDIC to defeat debtors' otherwise valid affirmative defenses, "such as contributory negligence, laches, waiver, interference with contract performance, failure of consideration and set off."<sup>67</sup> The Supreme Court created *D'Oench, Duhme* by relying in

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crises in the banking and S&L industries).

59. Reilly, *supra* note 29, at 176.

60. See Cherie Stephens Bock, Comment, *Alive, But Not Quite Kicking: Circuit Split Illustrates the Progressive Deterioration of the D'Oench, Duhme Doctrine*, 42 St. Louis L.J. 945, 950 (1998).

61. See Barry S. Zisman & Marguerite Woung, *Superpowers of the FDIC/RTC and their Availability to Third Parties*, 108 Banking L.J. 516, 517 (1991).

62. See Boteler, *supra* note 6, at 1170.

63. See Zisman & Woung, *supra* note 61, at 518.

64. 315 U.S. 447 (1942).

65. See Galves, *Might Does Not Make Right*, *supra* note 6, at 1327-28.

66. The FDIC protection as a holder in due course ("HDC") is one significant common law extension of the *D'Oench, Duhme* doctrine. See *Gunter v. Hutcheson*, 674 F.2d 862, 868 (11th Cir. 1982). An HDC takes a negotiable instrument free from all claims and defenses. See Bock, *supra* note 60, at 952 n.76. The FDIC does not qualify for holder in due course status as defined by the Uniform Commercial Code ("UCC") for two reasons. First, it does not acquire the failed depository institution's assets for value in the regular course of business, and second, the UCC provision exempts bulk sales. See Galves, *Might Does Not Make Right*, *supra* note 6, at 1352. The rule instead gives HDC status to the FDIC when it acquires a note in a P&A "for value, in good faith, and without actual knowledge of . . . fraud." *Gunter*, 674 F.2d at 873. The HDC status immunizes the FDIC against defenses including waiver, estoppel, laches, fraud in the factum, usury and failure of accord and satisfaction. See J. Michael Echevarria, *A Precedent Embalms a Principle: The Expansion of the D'Oench, Duhme Doctrine*, 43 Cath. U. L. Rev. 745, 774 (1994); Galves, *Might Does Not Make Right*, *supra* note 6, at 1353.

67. See Dennis & Simon, *supra* note 38, at 1319.



part on the policy interests of the FDIC as insurer of the nation's banks.<sup>68</sup>

*D'Oench, Duhme* originated from the 1942 Supreme Court case *D'Oench, Duhme & Co. v. FDIC*.<sup>69</sup> The FDIC initiated a lawsuit in federal court in Missouri to collect on a demand note executed by D'Oench, Duhme at an Illinois bank.<sup>70</sup> The court had subject matter jurisdiction under the Federal Reserve Act.<sup>71</sup> As a defense, D'Oench, Duhme argued that it executed the note with the understanding that the note would not be called for payment.<sup>72</sup> Although the bank did not enter this side agreement into its records, the receipts for the notes memorialized the understanding.<sup>73</sup> The parties executed the note so that an earlier, bad loan would appear on the bank's records as a good asset.<sup>74</sup> The secret "side agreement" was asserted as a defense against the FDIC's suit to collect the note.<sup>75</sup>

The Supreme Court decided *D'Oench, Duhme* after *Erie v. Tompkins*,<sup>76</sup> which dispensed with the application of federal general common law.<sup>77</sup> To justify the creation of federal common law after *Erie*,<sup>78</sup> the court distinguished *Erie*, which was a case in diversity<sup>79</sup> from *D'Oench, Duhme* which was a federal question case.<sup>80</sup> Justice Douglas, writing for the majority, held that federal law provided the rule of decision and then created a federal common law rule of estoppel.<sup>81</sup> Consequently, the Court rejected D'Oench, Duhme's defense and voided the secret agreement.<sup>82</sup> Douglas fashioned his holding in light of the goals animating the Federal Reserve Act, which were "to protect [the FDIC], and the public funds which it administers, against misrepresentations as to the securities or other

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68. See Galves, *Might Does Not Make Right*, *supra* note 6, at 1346 (noting that *D'Oench, Duhme* reflected federal policy to insure "integrity" of the FDIC fund).

69. 315 U.S. 447 (1942).

70. *See id.* at 453.

71. *See id.* at 455-56.

72. *See id.* at 454.

73. *See id.*

74. *See id.* at 456.

75. *See id.*

76. 304 U.S. 64 (1938).

77. *See id.* at 78.

78. *See D'Oench, Duhme*, 315 U.S. at 455.

79. The diversity jurisdiction of the federal court extends to cases between citizens of different states. *See Black's Law Dictionary* 477 (6th ed. 1990); *infra* note 111 and accompanying text.

80. *See supra* note 71 and accompanying text.

81. *See D'Oench, Duhme*, 315 U.S. at 459.

82. *See id.* (affirming judgment to enforce the note despite secret agreement defense by citing principles such as "the federal policy evidenced in this Act to protect [the FDIC], a federal corporation, from misrepresentations made to induce or influence the action of respondent, including misstatements as to the genuineness or integrity of securities in the portfolios of banks which it insures or to which it makes loans").

assets in the portfolios of the banks which [the FDIC] insures.”<sup>83</sup> As additional justification for the need to create this estoppel doctrine, Justice Douglas noted that “[t]he genuineness of assets ostensibly held by a bank is certainly germane to a determination of solvency.”<sup>84</sup> The Supreme Court, therefore, acknowledged the importance of the public interest in a stable banking industry and a solvent federal insurance fund when it created common law in the *D’Oench, Duhme* decision.

#### D. *The Role of Private Parties as Asset Purchasers from the FDIC*

Through P&As and bulk sales of assets, the FDIC used private funds to soften the blow to the insurance fund as a result of the massive failures in the banking industry. The FDIC and the RTC sold private parties distressed assets in bulk such as promissory notes and debt obligations.<sup>85</sup> Asset purchasers were comprised of individual investors, individuals that pooled funds, and institutional investors such as investment banks, brokerage houses and financial institutions.<sup>86</sup>

Because third party purchasers of assets constitute an essential part of P&As, some courts have readily extended the benefits of *D’Oench, Duhme* to private parties.<sup>87</sup> This follows the trend of the expansion of *D’Oench, Duhme* and related statutory<sup>88</sup> and common law<sup>89</sup>

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83. *Id.* at 457.

84. *Id.* at 460.

85. See Fred Galves, *FDIC and RTC Special Powers in Failed Bank Litigation*, 22 Colo. Law. 473, 473 (1993) [hereinafter Galves, *Special Powers*].

86. See Galves, *Might Does Not Make Right*, *supra* note 6, at 1362.

87. See *id.*

88. In 1950, as part of the Federal Deposit Insurance Act, Congress codified various aspects of the *D’Oench, Duhme* decision in what is now 12 U.S.C. § 1823(e). See Statement of Policy Regarding Federal Common Law and Statutory Provisions Protecting FDIC, as Receiver or Corporate Liquidator, Against Unrecorded Agreements or Arrangements of a Depository Institution Prior to Receivership, 62 Fed. Reg. 5984 (1997) [hereinafter Statement of Policy]. While *D’Oench, Duhme* is a rule of estoppel, § 1823(e) is a statute of frauds. See Galves, *Special Powers*, *supra* note 85, at 473. Satisfying § 1823(e)’s recording requirements allows borrowers to assert the validity of any side-agreements made with banks in the event of a bank failure. 12 U.S.C. § 1823(e) states:

Agreements against interests of Corporation.

(1) In general. No agreement which tends to diminish or defeat the interest of the Corporation in any asset acquired by it under this or 11 [12 USCS § 1821], either as security for a loan or by purchase or as receiver of any insured depository institution, shall be valid against the Corporation unless such agreement—

(A) is in writing,

(B) was executed by the depository institution and any person claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the depository institution,

(C) was approved by the board of directors of the depository institution or its loan committee, which approval shall be reflected in the minutes of said board or committee, and

counterparts to the FDIC in all of its regulatory capacities and to transferee banks.<sup>90</sup> Courts have upheld the exercise of FDIC common law powers by private parties to ensure that the FDIC can market the assets of a failed depository institution.<sup>91</sup> Because there are no hidden defenses derived from unrecorded side agreements when *D'Oench, Duhme* is asserted, these assets are neither risky nor undesirable purchases.<sup>92</sup> Courts also believed that because purchasers also need to value the assets of the failed financial institutions accurately, third parties should possess the same common law protections as the FDIC.<sup>93</sup> FDIC bank examiners and private entities that purchase assets from the FDIC equally rely on the accuracy of the records of depository institutions.<sup>94</sup> These courts believed that financial institutions would not enter into P&As without *D'Oench, Duhme* protection.<sup>95</sup>

As another matter, the majority courts found no legitimate reason to let debtors resurrect defenses abrogated by *D'Oench, Duhme* once the FDIC has transferred the note to a third party.<sup>96</sup> Because the

(D) has been, continuously, from the time of its execution, an official record of the depository institution.

12 U.S.C. § 1823(e)(1994).

89. See *supra* note 66.

90. See *Campbell Leasing, Inc. v. FDIC*, 901 F.2d 1244, 1249 (5th Cir. 1990) (extending federal holder in due course status to transferees); *Bell & Murphy & Assocs. v. Interfirst Bank Gateway, N.A.*, 894 F.2d 750, 754-55 (5th Cir. 1990) (extending status to bridge banks); *Porras v. Petroplex Sav. Ass'n.*, 903 F.2d 379, 380 (5th Cir. 1990) (extending *D'Oench, Duhme* to Federal Savings and Loan Insurance Corporation assignee); *FSLIC v. Consolidated Fed. Sav. Bank*, 918 F.2d 557, 560 (5th Cir. 1990) (same); *FDIC v. Newhart*, 892 F.2d 47, 51 (8th Cir. 1989) (extending federal holder in due course status to private party relying on *D'Oench, Duhme* doctrine, 12 U.S.C. § 1823(e) and *Gunter v. Hutcheson*); cf. *Garrett v. Coastal Fin. Management Co.*, 765 F. Supp. 351, 352-53 (S.D. Tex. 1990) (making *D'Oench, Duhme* and § 1823(e) defenses available to subsidiaries of failed financial institutions).

91. See *Newhart*, 892 F.2d at 50.

92. See Galves, *Special Powers*, *supra* note 85, at 478 (speculating about the FDIC's difficulty in finding third parties willing to purchase risky assets); Michael W. Lillie, *Federal Superpowers in Failed Banking Litigation: The D'Oench, Duhme Doctrine*, 20 Colo. Law. 427, 432 (1991).

93. See Galves, *Might Does Not Make Right*, *supra* note 6, at 1382-83.

94. See *id.* at 1362-63.

95. Cf. *Newhart*, 892 F.2d at 50 (discussing extension of FDIC's common law HDC status). The *Newhart* court argues:

[A] contrary result would emasculate the policy behind § 1823(e) of promoting purchase and assumption transactions. If holder in due course status did not run with the notes acquired by the FDIC in purchase and assumption transactions, the market for such notes would be smaller, which would have a deleterious effect on the FDIC's ability to protect the assets of failed banks.

*Id.*

96. See *Willow Tree Inv. v. Wagner*, 453 N.W. 2d 641, 644 (Iowa 1990) ("It would be contrary to these stated goals to allow a party to revive claims against the insolvent institution simply because the FDIC subsequently transferred the note to a third party.").

transfer of such obligations is a common practice, the fact that the transferee is a holder in due course is neither inequitable nor an unfair surprise to the maker of the note.<sup>97</sup> Lastly, the enormous cost of the bailout of the failed S&Ls in the 1980s gave courts another practical reason to extend these superpowers to third parties.<sup>98</sup> Without the sale of these assets, the FDIC and RTC would have faced the insurmountable task of litigating all the claims on the billions of dollars of assets it held.<sup>99</sup>

The next part will examine federal court jurisdiction and will describe the Congressional grant of the FDIC's federal jurisdiction in title 12 § 1819(b)(2)(A).

## II. FEDERAL COURT JURISDICTION

This part explores the foundations of the subject matter jurisdiction of federal courts. Subject matter jurisdiction refers to a court's ability to hear and decide "cases of the general cases or category," with respect to the particular proceeding before it.<sup>100</sup> After setting out a constitutional and statutory analysis of federal jurisdiction, this part will explore the FDIC's statutory grant of jurisdiction under FIRREA.

### A. Constitutional Power and Jurisdictional Limits

Article III of the Constitution states that "[t]he judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority."<sup>101</sup> Chief Justice John Marshall broadly interpreted this grant of judicial power in *Osborn v. Bank of the United States*,<sup>102</sup> where he stated, "[o]riginal jurisdiction, so far as the constitution gives a rule, is co-extensive with the judicial power."<sup>103</sup> In *Osborn*, Marshall announced that federal jurisdiction

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97. See *Campbell Leasing, Inc. v. FDIC*, 901 F.2d 1244, 1250 (5th Cir. 1990). In *Campbell Leasing*, the court wrote:

A negotiable instrument is subject to transfer at any time and the maker must always be aware that the transferee may be a holder in due course. From the maker's view, there is no difference between his bank failing and the note going to the . . . FDIC, and his bank failing after selling the note to a holder in due course.

*Id.*

98. See Bock, *supra* note 60, at 958 ("With the acceleration of bank and thrift failures in the early 1980s, however, Congress began to embark on enlarging the *D'Oench* doctrine to further protect the FDIC's interest in safeguarding the insurance fund.").

99. See Zisman & Woung, *supra*, note 61, at 516.

100. Black's Law Dictionary 854 (6th ed. 1990).

101. U.S. Const. art. III, § 2.

102. 22 U.S. (9 Wheat.) 738 (1824).

103. *Osborn*, 22 U.S. (9 Wheat.) at 821.

exists where federal law forms "an ingredient of the original cause."<sup>104</sup>

The Constitutional grant is broad, but the actual exercise of federal court power to hear a case depends on statutory law.<sup>105</sup> The Constitution empowers Congress to control the scope of lower court jurisdiction.<sup>106</sup> Congress has never extended federal jurisdiction to the full limits articulated in *Osborn*.<sup>107</sup> The federal question<sup>108</sup> and diversity statutes<sup>109</sup> are the two primary grants conferring original jurisdiction to the federal courts. The general federal question statute closely tracks the language of Article III, giving a court subject matter jurisdiction over "all civil actions arising under the Constitution, laws or treaties of the United States."<sup>110</sup> Diversity jurisdiction refers to the jurisdiction of federal courts over citizens of different states.<sup>111</sup> Under § 1332, the requisite amount in controversy must also be met.<sup>112</sup> Jurisdiction in the lower federal courts is further limited by the amount-in-controversy requirement<sup>113</sup> and the narrow interpretation of the scope of the Congressional grant in the federal question statute.<sup>114</sup>

### B. Policy Reasons for Jurisdictional Limits

As a general matter, federal courts are courts of limited jurisdiction.<sup>115</sup> In contrast, most state courts are courts of general jurisdiction and may hear matters that include all causes of action unless barred by statute.<sup>116</sup> State courts also enjoy concurrent jurisdiction with federal courts over all matters, with the exception of actions arising from specific federal statutes that establish exclusive

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104. *Id.* at 823.

105. See *Finley v. United States*, 490 U.S. 545, 548 (1989).

106. See U.S. Const. art. I, § 8, cl. 9 ("The Congress shall have Power . . . [t]o constitute Tribunals inferior to the supreme Court.").

107. See, e.g., Gene R. Shreve & Peter Raven-Hansen, *Understanding Civil Procedure* 103 (1996) ("Congress has never vested [lower federal courts] with as much subject matter jurisdiction as Article III permits."); Charles Alan Wright, *Law of Federal Courts* § 10 at 40-47 (1994) (discussing Congressional discretion to confer jurisdiction on lower federal courts).

108. See 28 U.S.C. § 1331 (1994). This version of the general federal question statute was enacted in 1976. See Richard H. Fallon, Jr. et al., *Hart and Weschler's The Federal Courts and The Federal System* 883 (4th ed. 1996).

109. See 28 U.S.C. § 1332.

110. *Id.* § 1331. "The district courts shall have original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of the United States." *Id.* § 1331; see Shreve & Raven-Hansen, *supra* note 107, at 105.

111. See *Black's Law Dictionary* 477 (6th ed. 1990).

112. See *id.*

113. See Shreve & Raven-Hansen, *supra* note 107, at 104. The amount in controversy is the amount of alleged damages claimed or relief demanded by the plaintiff. See *Black's Law Dictionary* 83 (6th ed. 1990).

114. See Erwin Chermersky, *Federal Jurisdiction* § 5.2, at 264 (3d ed. 1999); *supra* note 107 and accompanying text.

115. See Chermersky, *supra* note 114, § 5.1 at 257.

116. See *id.*

federal jurisdiction.<sup>117</sup> Federal courts exist so that the federal government can protect federal rights and enforce its own laws.<sup>118</sup>

Federalism concerns underlie the limited scope of the jurisdictional grant conferred to federal district courts. The federal forum created by these statutes exists as a prophylactic against perceived dangers that may arise if state courts hear cases in diversity or those that arise under federal law.<sup>119</sup> Underlying this justification is the view that state courts are less desirable forums in which to achieve federal aims.<sup>120</sup> This distrust of state courts is comprised of several elements. State courts may lack the expertise to interpret and apply federal law.<sup>121</sup> A state court's parochial interest may influence actions involving parties who are citizens of different states<sup>122</sup> or the federal government.<sup>123</sup> Some commentators also believe that uniformity of federal law is better achieved through a federal district court system.<sup>124</sup>

### C. Discretionary Exercise of Federal Jurisdiction

Economy and efficiency, along with convenience and fairness to litigants, are administrative and equitable elements that also shape the exercise of federal jurisdiction.<sup>125</sup> Courts must consider these aspects when parties wish to bring additional claims or parties to an action.<sup>126</sup>

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117. *See id.*

118. *See* Shreve & Raven-Hansen, *supra* note 107, at 104 (describing federal jurisdiction as "premised on the belief that federal courts should have the authority to expound and apply federal law because of their expertise in that law, their relative insulation from local majoritarian pressures (and correspondingly more protective attitude toward federal rights), and their ability to give federal law more uniform application than state courts").

119. *See id.*

120. *See id.*

121. *See* Chermersky, *supra* note 114, § 5.2.1 at 263.

122. *See* Bank of United States v. Deveaux, 9 U.S. (5 Cranch.) 61, 87 (1809); Chermersky, *supra* note 114, § 5.3 at 289.

123. *See* Osborn v. Bank of the United States, 22 U.S. (9 Wheat.) 738, 849 (1824) ("[I]f the Courts of the United States cannot rightfully protect the agents who execute every law authorized by the constitution, from the direct action of State agents in the collection of penalties, they cannot rightfully protect those who execute any law.").

124. *See* Shreve & Raven-Hansen, *supra* note 107, at 104.

125. *See* United Mine Workers of Am. v. Gibbs, 383 U.S. 715, 724-26 (1966).

126. The exercise of a court's jurisdiction over these additional parties and claims is codified in the supplemental jurisdiction statute, 28 U.S.C. § 1367.

These concerns of economy, fairness, and efficiency also affect a district court's exercise of discretion to decline cases properly within the jurisdiction of federal courts. *See* Wright, *supra* note 107, § 52, at 323. When there are related or even parallel proceedings in federal and state courts, sometimes a party urges a federal court to decline to proceed. The abstention doctrine is based in case law and there are exceptional instances where federal courts decline to exercise their jurisdiction. *See* Colorado River Water Conservation Dist. v. United States, 424 U.S. 800, 818-20 (1976) (enforcing a stay when parallel proceedings occur in federal court only in "exceptional" circumstances); *Younger v. Harris*, 401 U.S. 37, 53 (1971) (concerning state criminal proceedings); *Burford v. Sun Oil Co.*, 319 U.S. 315, 333-34 (1943) (declining to interfere in state administrative proceedings); *Railroad Comm'n of*

This section focuses on the supplemental jurisdiction statute as an example of the discretionary exercise of federal court jurisdiction.

### 1. Constitutional Background

*Finley v. United States*<sup>127</sup> and *United Mine Workers of America v. Gibbs*<sup>128</sup> are two important cases that shaped the supplemental jurisdiction statute and laid the foundations for the contemporary debate on the scope of modern federal court jurisdiction.

*Gibbs* first addressed the Constitutional "power"<sup>129</sup> of a federal court to hear pendent claims, in other words, "nonfederal claims between parties litigating other matters properly before the court."<sup>130</sup> The Court noted that Article III's jurisdictional grant extended to state claims related to a federal claim with "substance sufficient to confer subject matter jurisdiction on the court."<sup>131</sup> Together, the federal and related state claims comprise "one constitutional 'case.'"<sup>132</sup> *Gibbs* described related claims as claims that "derive from a common nucleus of operative fact."<sup>133</sup>

*Gibbs* relied on the view of federal court practice espoused by the Federal Rules of Civil Procedure. It characterized the tenor of the Federal Rules as "entertaining the broadest possible scope of action consistent with fairness to the parties; joinder of claims, parties and remedies is strongly encouraged."<sup>134</sup> After discussing the authority of the court to hear non-federal claims that are deemed part of the same constitutional case, *Gibbs* then announced that the exercise of such jurisdiction is discretionary and guided by considerations of "judicial economy, convenience and fairness to litigants."<sup>135</sup> According to *Gibbs*, federal courts are also to avoid issuing needless decisions of state law in the interests of comity.<sup>136</sup>

The Supreme Court's decision in *Finley* placed in doubt much of the case law following the approach to pendent jurisdiction outlined in *Gibbs*. *Finley* cautioned courts against the exercise of jurisdiction absent affirmative Congressional authorization.<sup>137</sup> The *Finley* decision questioned the ability of a plaintiff to add pendent parties, parties

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Texas v. Pullman Co., 312 U.S. 496, 501 (1941) (deferring to state court in order to allow state to interpret a state statute subject to Constitutional challenge).

127. 490 U.S. 545 (1989).

128. 383 U.S. 715 (1966).

129. *Gibbs*, 383 U.S. at 725.

130. *Finley*, 490 U.S. at 548.

131. *Gibbs*, 383 U.S. at 725.

132. *Id.*

133. *Id.*

134. *Id.* at 724.

135. *Id.* at 726.

136. *See id.*

137. *See Finley v. United States*, 490 U.S. 545, 549 (1989).

“over whom no independent basis of jurisdiction exists,”<sup>138</sup> to an action based on exclusive federal court jurisdiction under the Federal Tort Claims Act.<sup>139</sup> Justice Scalia wrote on behalf of the Court, and cast doubt upon the constitutionality of this exercise of jurisdiction.<sup>140</sup> He claimed that Congressional authority to exercise pendent party jurisdiction was absent.<sup>141</sup> In defense of this result, he urged a more clear indication from Congress: “[w]hat is of paramount importance is that Congress be able to legislate against a background of clear interpretive rules, so that it may know the effect of language it adopts.”<sup>142</sup> The decision prompted the enactment of such a provision in 1990.

## 2. Enactment of § 1367

The supplemental jurisdiction statute, 28 U.S.C. § 1367,<sup>143</sup> allows claims without an independent basis for federal jurisdiction to accompany a jurisdictionally sufficient claim into federal court when they are part of one “constitutional case.”<sup>144</sup> Supplemental jurisdiction does not extend to all related claims that originate from the same nucleus of operative fact. For example, § 1367(b) denies federal supplemental jurisdiction when a case is in federal court because of diversity of citizenship if the additional parties to be added would not meet the requirements of § 1332.<sup>145</sup>

Section 1367(c) lists four factors that guide the discretionary exercise of supplemental jurisdiction.<sup>146</sup> The first two factors address issues of federal courts interpreting state law. A court can elect not to exercise jurisdiction where novel or complex state law issues exist in related claims or when state law claims predominate over those claims that have original jurisdiction.<sup>147</sup> Under the third factor, when “the district court has dismissed all claims over which it has original

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138. *Id.* at 551.

139. *See id.* at 546-47.

140. *See id.* at 549.

141. *See id.*

142. *Id.* at 556.

143. 28 U.S.C. § 1367(a) provides in relevant part:

Except as provided in subs (b) and (c) or as expressly provided otherwise by Federal statute, in any civil action of which the district courts have original jurisdiction, the district courts shall have supplemental jurisdiction over all other claims that are so related to claims in the action within such original jurisdiction that they form part of the same case or controversy under Article III of the United States Constitution. Such supplemental jurisdiction shall include claims that involve the joinder or intervention of additional parties.

28 U.S.C. § 1367(a) (1994).

144. *United Mine Workers of Am. v. Gibbs*, 383 U.S. 715, 725 (1966).

145. *See* 28 U.S.C. § 1367(b).

146. *See id.* § 1367(c)(1)-(4).

147. *See id.*



jurisdiction," a court may decline jurisdiction in its discretion.<sup>148</sup> Finally, under § 1367(c)(4), discretion may be exercised when "exceptional circumstances" or "other compelling reasons" are present.<sup>149</sup>

There is conflict among the circuits<sup>150</sup> as to whether § 1367(c) leaves intact the scope of a court's discretion as articulated in *Gibbs*<sup>151</sup> and *Carnegie-Mellon University v. Cohill*.<sup>152</sup> Although legislative history indicates that § 1367 aimed to codify and restore pendent and ancillary jurisdiction to its pre-*Finley* status,<sup>153</sup> the statute does not adopt the discretionary analysis of *Gibbs*.<sup>154</sup> Some commentators have argued that § 1367 broadens a federal court's ability to exercise supplemental jurisdiction because § 1367(c)(1)-(4) limits discretion to decline jurisdiction.<sup>155</sup>

The Supreme Court discussed its understanding of the legislative intent of § 1367(c) in its *City of Chicago v. International College of Surgeons*<sup>156</sup> decision. Its interpretation supports the theory that Congress codified *Gibbs* in § 1367(c).<sup>157</sup> In *International College of Surgeons*, the Court incorporated *Gibbs* and *Cohill* when it discussed the policies guiding the proper exercise of discretion under § 1367.<sup>158</sup> The discretion to exercise supplemental jurisdiction allows a federal court to "consider and weigh in each case, at every stage of litigation,

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148. *Id.* § 1367(c)(3).

149. *Id.* § 1367(c)(4).

150. See John B. Oakley, *Prospectus for the American Law Institute's Federal Judicial Code Revision Project*, 31 U.C. Davis L. Rev. 855, 943 (1998) (describing the division between the Seventh Circuit and Ninth Circuit approaches). Oakley writes, "[t]here are manifest discrepancies between *Gibbs*' standards and the text of subsection 1367(c)." *Id.*

151. *United Mine Workers of Am. v. Gibbs*, 383 U.S. 715, 726 (1966) (listing "judicial economy, convenience and fairness to litigants").

152. 484 U.S. 343, 350 (1988) (listing values such as "economy, convenience, fairness and comity").

153. See *supra* notes 127-36 and accompanying text.

154. See Jon D. Corey, Comment, *The Discretionary Exercise of Supplemental Jurisdiction Under the Supplemental Jurisdiction Statute*, 1995 BYU L. Rev. 1263, 1272-82, 1288-95 (1995).

155. See *id.* at 1282-87. Other commentators attribute the conflict to the Practice Commentary of Professor David Siegel, who identifies the abstention doctrine as the source of the discretionary factors in the subsection of § 1367(c). See Joseph N. Akrotirianakis, Comment, *Learning to Follow Directions: When District Courts Should Decline to Exercise Supplemental Jurisdiction Under 28 U.S.C. § 1367(c)*, 31 Loy. L.A. L. Rev. 995, 1007 (1998). They believe that Siegel incorrectly describes the legislative history of § 1367(c) by failing to emphasize *Gibbs* as source of the policy and the language of the § 1367(c) subsections. See *id.* at 1032 ("Though the *Gibbs* decision antedates the enactment of § 1367, it discussed the policies underlying the doctrine of pendent jurisdiction, and its language later provided the very foundation on which Congress built our supplemental jurisdiction statute.").

156. 522 U.S. 156, 165 (1997).

157. See *id.*; see James E. Pfander, *Supplemental Jurisdiction and Section 1367: The Case for a Sympathetic Textualism*, 148 U. Pa. L. Rev. 109, 122 n.47 (1999).

158. See *International College of Surgeons*, 522 U.S. at 164-65.

the values of judicial economy, convenience, fairness and comity.”<sup>159</sup> The Court mentioned that the supplemental jurisdiction statute codified those principles.<sup>160</sup>

#### D. *Determining Jurisdiction—Time of Filing Rule*

The time-of-filing rule takes a snapshot of events at the time a complaint is filed in federal court to determine whether proper federal jurisdiction exists. In cases of removal from state court, the district court analyzes whether it has subject matter jurisdiction as of the time of the filing of the removal motion.<sup>161</sup> After a court finds that it has proper authority to hear a case, subsequent events cannot divest the court of jurisdiction. These events may include destruction of complete diversity following a change in domicile or the parties, or an amendment or dismissal of a claim that reduces the amount in controversy below the statutory threshold.<sup>162</sup>

The time-of-filing rule prevents strategic behavior by parties to defeat federal jurisdiction once litigation has begun.<sup>163</sup> For example, an amended pleading that lowers the amount in controversy below the statutory requirement does not divest the federal court of authority to hear that case.<sup>164</sup> A plaintiff's efforts to remand an action to state court by amending the pleading to lower the jurisdictional amount would fail. The time-of-filing rule also minimizes disruptions from repeated challenges to the court's subject matter jurisdiction and lends

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159. *Id.* at 173 (citing *Carnegie-Mellon Univ. v. Cohill*, 484 U.S. 343, 350, 357 (1988)).

160. *See id.* Finally, the Court treated abstention as a separate and additional justification for a federal court to decline or stay the exercise of jurisdiction over state law claims, and therefore made it less likely that abstention was the doctrinal source for the § 1367(c) factors. *See id.* at 174. The court noted that abstention may be proper in situations “even if the jurisdictional prerequisites are otherwise satisfied.” *Id.*

161. *See Grinnell Mut. Reins. Co. v. Shierk*, 121 F.3d 1114, 1117 (7th Cir. 1997) (“A defect in diversity jurisdiction exists, if at all, only when a case is filed in federal court or removed to federal court from state court.”). In cases where federal question jurisdiction is alleged, the defendant must show that, in accord with the well-pleaded complaint rule, a federal question is an essential ingredient of the complaint. *See Franchise Tax Board v. Const. Laborers Vacation Trust for S. Cal.*, 463 U.S. 1, 10 (1983).

162. *See, e.g., Bermudez v. Industrial Siderurgica, Inc.*, 672 F. Supp. 57, 59 (D.P.R. 1987) (“It is well established that a federal court does not lose diversity jurisdiction which was founded at the commencement of the action although domiciliary of one of the parties has changed, substitution by a non-diverse person, or the amount recovered fell below the \$10,000.” (citation omitted)).

163. *See New Rock Asset Partners v. Preferred Entity Advancements, Inc.*, 101 F.3d 1492, 1503 (3d Cir. 1996).

164. *See St. Paul Mercury Indem. Co. v. Red Cab Co.*, 303 U.S. 283, 289-90 (1938). Likewise, if a judgment awarded turns out to be less than the amount in controversy, a court still retains diversity jurisdiction because the amount in controversy was pled in good faith at the time of filing. *See Grinnell*, 121 F.3d at 1116.

stability and certainty to litigation.<sup>165</sup> The rule prevents undue delay in litigation and unnecessary appeals.<sup>166</sup> The Supreme Court also noted that extra-judicial concerns require the rule because "[a] contrary rule could well have the effect of deterring normal business transactions during the pendency of what might be lengthy litigation."<sup>167</sup>

There are no references to the time-of-filing rule in any jurisdictional statute.<sup>168</sup> However, the principle has an illustrious history and there is ample support for the rule in case law.<sup>169</sup> According to Chief Justice Marshall, "[i]t is quite clear, that the jurisdiction of the Court depends upon the state of things at the time of the action brought, and that after vesting, it cannot be ousted by subsequent events."<sup>170</sup> Supreme Court decisions have affirmed its application in cases dealing with changes in the amount in controversy<sup>171</sup> and diversity of citizenship<sup>172</sup> that occur subsequent to filing in federal court.

It is unclear, however, whether the time-of-filing rule has withstood the rigors of a constitutional analysis. Justice Scalia challenged its status as an "ironclad *per se* rule without exceptions" and questioned whether "events at the initiation of the lawsuit are the only proper jurisdictional reference point."<sup>173</sup> Indeed, in exceptional circumstances, a safety valve exists and the time-of-filing rule is not

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165. See Charles Alan Wright, et al., 13B Federal Practice and Procedure § 3608, at 453 (2d ed. 1984).

166. See *Saadeh v. Farouki*, 107 F.3d 52, 57 (D.C. Cir. 1997) ("Were it necessary to track changes of citizenship throughout litigation, courts would face potentially difficult burdens of either holding cases in abeyance for the diversity requirements to be satisfied or, alternatively, repeatedly adjudicating challenges to previous determinations that diversity jurisdiction existed.").

167. *Freeport-McMoRan, Inc. v. K N Energy, Inc.*, 498 U.S. 426, 428-29 (1991) (*per curiam*).

168. See Wright et al., *supra* note 165, § 3608 at 452.

169. See, e.g., *Freeport*, 498 U.S. at 428 ("We have consistently held that if jurisdiction exists at the time an action is commenced, such jurisdiction may not be divested by subsequent events."); see also *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 569-70 n.4 (1992) (Blackmun J., dissenting) (affirming the "longstanding rule that jurisdiction is to be assessed under the facts existing when the complaint is filed"); *Newman-Green, Inc. v. Alfonzo-Larrain*, 490 U.S. 826, 830 (1989) ("The existence of federal jurisdiction ordinarily depends on the facts as they exist when the complaint is filed."); *Smith v. Sperling*, 354 U.S. 91, 93 n.1 (1957) ("The rationale, that jurisdiction is tested by the facts as they existed when the action is brought, is applied to a situation where a party dies and a nondiverse representative is substituted."); *St. Paul Mercury Indem. Co.*, 303 U.S. at 289-90 ("Events occurring subsequent to the institution of suit which reduce the amount recoverable below the statutory limit do not oust jurisdiction."); *Saadeh*, 107 F.3d at 57 (holding that a party that became a United States citizen by the time of trial and possibly changed domicile could not cure the jurisdictional defect at outset of case).

170. *Mullen v. Torrance*, 22 U.S. (9 Wheat.) 537, 539 (1824).

171. See *St. Paul Mercury Indem. Co.*, 303 U.S. at 289.

172. See *Mullen*, 22 U.S. (9 Wheat.) at 539.

173. *Lujan*, 504 U.S. at 598-99 n.4 (Scalia, J., dissenting).

mechanically applied. In two cases, for example, although no federal court jurisdiction appeared at the outset of the trial, the Supreme Court refused to dismiss or remand cases when federal jurisdiction later vested or was repaired. First, in *Newman-Green, Inc. v. Alfonzo-Larrain*,<sup>174</sup> the Supreme Court held that it was not an abuse of discretion for the appellate court to dismiss a party that spoiled complete diversity.<sup>175</sup> At oral argument on his own motion, Judge Easterbrook of the Court of Appeals for the Seventh Circuit questioned the presence of diversity jurisdiction.<sup>176</sup> One of the respondents was a United States citizen who was stateless for the purposes of the diversity statute because he was domiciled in Venezuela.<sup>177</sup> Instead of dismissing the case for a lack of subject matter jurisdiction, or remanding the case to the district court, the Court of Appeals granted petitioner Newman-Green's motion to amend the complaint to drop the non-diverse respondent.<sup>178</sup> The Supreme Court concluded that the dismissal did not prejudice any of the parties and that the non-diverse party was dispensable.<sup>179</sup> They noted that "[n]othing but a waste of time and resources would be engendered by remanding to the District Court or by forcing these parties to begin anew."<sup>180</sup> In *Caterpillar Inc. v. Lewis*,<sup>181</sup> the parties were not in complete diversity when the claim was removed to federal court over the objection of the plaintiff.<sup>182</sup> By the time the case reached litigation, a settlement had induced the non-diverse party to withdraw.<sup>183</sup> The Court of Appeals vacated the District Court judgment because it found that diversity was not complete when Caterpillar removed the case to federal court.<sup>184</sup> Efficiency concerns, particularly the cost to both the federal and state courts of retrying a case where final judgment was entered, were key to the Court's decision to reverse the appellate court and uphold the judgment of the district court.<sup>185</sup> The Supreme Court has disregarded the time-of-filing rule, where in the interests of finality and efficiency, its application would waste the time and resources of the courts and the parties.

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174. 490 U.S. 826 (1989).

175. See *id.* at 833 (allowing Court of Appeals to dismiss a dispensable non-diverse party under Rule 21 in order to retroactively confer jurisdiction).

176. See *id.* at 828.

177. See *id.*

178. See *id.* at 829.

179. See *id.*

180. *Id.* at 838.

181. 519 U.S. 61 (1996).

182. See *id.* at 64.

183. See *id.*

184. See *id.* at 67.

185. See *id.* at 77 ("To wipe out the adjudication postjudgment, and return to state court a case now satisfying all federal jurisdictional requirements, would impose an exorbitant cost on our dual court system, a cost incompatible with the fair and unprotracted administration of justice.").

E. *Basis for FDIC Jurisdiction*

Under 12 U.S.C. § 1819(b)(2)(A), "all suits of a civil nature at common law or in equity," in which the FDIC appears in any capacity, "arise under the laws of the United States."<sup>186</sup> All actions in which the FDIC is a party, whether as a plaintiff or defendant, fall under federal question jurisdiction. The statute lists one exception to this broad grant of federal jurisdiction.<sup>187</sup> Congress withheld jurisdiction when the FDIC acts as a receiver of a state-insured depository institution, and it is not a plaintiff in an action brought under state law that "involves only the preclosing rights against the State insured depository institution" or obligations of the institution to its depositors, creditors or stockholders.<sup>188</sup> In addition, after the enactment of FIRREA, the FDIC gained agency status.<sup>189</sup> Under 28 U.S.C. § 1345, Congress conferred original jurisdiction on district courts in "civil actions, suits or proceedings" brought by agencies of the United States recognized under the statute.<sup>190</sup>

Before FIRREA, statutory language did not recognize the FDIC as an agency of the United States under 28 U.S.C. § 1345. Section 1819(b)(1) was originally enacted as part of the FDIC's enabling legislation in 12 U.S.C. § 264(j) of the Banking Act of 1933.<sup>191</sup> The earliest version of the statute granting jurisdiction, former § 264(j), contained a provision authorizing the FDIC to "sue and be sued" in any federal or state court.<sup>192</sup> The Supreme Court affirmed the constitutionality of the Congressional grant of original jurisdiction in *D'Oench, Duhme & Co. v. FDIC*,<sup>193</sup> and again in *American National Red Cross v. S.G.*<sup>194</sup> Both *D'Oench, Duhme* and *Red Cross* affirmed that the "sue or be sued . . . in any court of law or equity, State or Federal" language in a federal charter was a sufficient ground on which to rest federal jurisdiction.<sup>195</sup> The majority opinion in *Red Cross* traced its reasoning to *Osborn v. Bank of United States*, where Justice Marshall found federal jurisdiction based on the bank's sue and be sued chartering language.<sup>196</sup> The propriety of the Congressional grant of FDIC jurisdiction under FIRREA therefore rests on a sound constitutional basis.

Section 1819(b)(2)(A) is a broad Congressional grant of federal

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186. 12 U.S.C. § 1819(b)(2)(A) (1994).

187. *See id.* § 1819(b)(2)(D).

188. *Id.*

189. *See id.* § 1819(b)(1).

190. 28 U.S.C. § 1345 (1994).

191. *See American Nat. Red Cross, v. S.G.*, 505 U.S. 247, 254 n.4. (1992).

192. *See D'Oench, Duhme & Co., v. FDIC*, 315 U.S. 447, 455 (1942).

193. *Id.* at 456.

194. 505 U.S. 247 (1992).

195. *D'Oench, Duhme*, 315 U.S. at 455; *Red Cross*, 505 U.S. at 254-55.

196. *Osborn v. Bank of the United States*, 22 U.S. (9 Wheat.) 738, 817 (1824).

jurisdiction.<sup>197</sup> Under § 1819, the FDIC can commence litigation in federal court or remove an action to federal court in any capacity, whether it is “stepping into the shoes” of a failed depository institution as a receiver or acting in its corporate capacity to recover assets for the deposit insurance fund.<sup>198</sup> In contrast to this clear Congressional grant, the status of federal jurisdiction when the FDIC sells assets of a failed bank to a non-diverse private party is an issue that has divided the circuit courts. The next part will describe the legal controversy.

### III. LEGAL CONTROVERSY

As part of its duties as receiver, or while acting in its capacity as an insurer, the FDIC may pursue litigation to collect assets from debtors that are owed to banks.<sup>199</sup> The FDIC regularly sells these assets to private parties as part of its strategy to recover the maximum value of these assets and minimize loss to the insurance fund.<sup>200</sup> A legal controversy arises when the FDIC transfers assets of a failed depository institution to a private party during pending litigation in federal court, leaving non-diverse remaining parties who assert only state law claims. Authorities disagree as to whether FIRREA allows the successor party to avoid remand to state court. This part discusses two approaches taken by federal courts to address this jurisdictional question.

#### A. *The Majority*

Courts in the majority have applied case law that extends FDIC common law and statutory powers under FIRREA to third party purchasers, holding that federal jurisdiction passes with assignment of the assets. The majority courts viewed private party purchasers as successors in interest to the FDIC. These courts have also invoked the time-of-filing rule to hold that once jurisdiction has been properly established, it does not disappear after a transfer in interest.

##### 1. Private Parties Inherit FDIC Superpowers

The majority courts determined that the transferees’ right to assert the *D’Oench, Duhme* doctrine justifies the preservation of federal jurisdiction after the FDIC is no longer a party to the case.<sup>201</sup> Just as policy reasons supported the extension of *D’Oench, Duhme* to private parties, “[t]he policy reasons for insuring federal jurisdiction over

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197. See *supra* note 186 and accompanying text.

198. See 12 U.S.C. § 1819(b)(2)(A) (1994).

199. See *supra* notes 54-84 and accompanying text.

200. See *supra* notes 85-86 and accompanying text.

201. See *FSLIC v. Griffin*, 935 F.2d 691, 696 (5th Cir. 1991).

cases involving the actions of failed thrifts continue when the FDIC is voluntarily dismissed as a party and the owner of the failed thrift's assets remains."<sup>202</sup> According to several courts, the grant of federal jurisdiction to the FDIC originated from a desire for the uniform application of FIRREA and the unhindered exercise of the FDIC's powers.<sup>203</sup> Because private parties may assert the FDIC's federal common law powers by virtue of assignment, courts still have an interest in the uniform application of these laws.

Majority courts also found support in FIRREA's "comprehensive scheme" for continuing federal jurisdiction in the action after the FDIC has assigned these assets and is no longer a party.<sup>204</sup> FIRREA reflects a clear "policy interest" to get the assets of failed financial institutions out of the FDIC's hands as quickly as possible.<sup>205</sup> By disposing of these assets, the insurance fund is protected, and taxpayers need not bear the burden of an insolvent depository institution. Hence, the transfers of these assets to private parties are "in the public interest."<sup>206</sup> For that reason, courts have decided that it would be contrary to FIRREA and against the public interest to make these transactions more costly by shuffling litigation between state and federal courts.<sup>207</sup>

## 2. The Time-of-Filing Rule

Courts in the majority have also held that jurisdiction is determined either at the time a claim is filed in federal court or at the time of its removal, and any events after the time of filing do not divest subject matter jurisdiction.<sup>208</sup> According to the courts, remand to state court

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202. *Id.*

203. *See, e.g., Mizuna, Ltd. v. Crossland Fed. Sav. Bank*, 90 F.3d 650, 657 (2d Cir. 1996) (discussing FIRREA's "sweeping powers"). *But see CIT, Inc. v. Willow St. Assocs.*, No. 93 Civ. 1201, 1997 U.S. Dist. LEXIS 12844, at \*18 (S.D.N.Y. Aug. 26, 1997) (noting that state courts are "up to [the] task" of interpreting common law *D'Oench, Duhme*).

204. *Mizuna*, 90 F.3d at 657.

205. *FDIC v. Bledsoe*, 989 F.2d 805, 811 (5th Cir. 1993).

206. *FDIC v. Four Star Holding Co.*, 178 F.3d 97, 101 (2d Cir. 1999).

207. *See CIT*, 1997 U.S. Dist. LEXIS 12844, at \*24. ("[T]he FDIC would be given the tools to come into federal court, and then, if it is able to serve its function by divesting itself of the assets at issue, the efforts expended by the litigants and federal judges could be wasted, as the litigation might well need to proceed again from scratch in state court."); *cf. Harding v. Bell*, 817 F. Supp. 1186, 1195 (D.N.J. 1993) (discussing why federal jurisdiction attaches in pre-receivership claims). *Harding* dealt with establishing jurisdiction in an action in federal court before the FDIC was appointed receiver. *See Harding*, 817 F. Supp. at 1188. In addition to relying on the time-of-filing rule, the court acknowledged that the Congressional intent behind the statutory scheme of FIRREA was to facilitate the smooth and efficient takeover and rehabilitation of failed depository institutions. *See id.* at 1195-96. When claims that may be "substantially underway" are dismissed only to return after the claims procedure is exhausted, such an efficient scheme is frustrated. *Id.*

208. *See Four Star*, 178 F.3d at 100-01; *FSLIC v. Griffin*, 935 F.2d 691, 696 (5th Cir.

would increase litigation costs and expend the court's resources.<sup>209</sup> Likewise, if jurisdiction were reassessed after a new party joined the action, there would be a disincentive for "normal business transactions" to take place during often lengthy litigation.<sup>210</sup> Therefore, under the time-of-filing rule, the transfer of assets from the FDIC to a private party does not divest a court's subject matter jurisdiction over the action, despite the fact that the remaining parties are non-diverse and the action only concerns state law claims.

### B. *The Minority*

Two cases provide an alternative analysis to the question of whether a federal court has subject matter jurisdiction after the FDIC transfers its assets to a private party during an ongoing litigation, leaving non-diverse parties who assert state law claims. In 1996, the Third Circuit adopted a contrary approach to the one employed by the only other court of appeals that had considered this question.<sup>211</sup> The court in *New Rock Asset Partners v. Preferred Entity Advancements, Inc.*<sup>212</sup> followed the reasoning of a Maine district court's decision in *Mill Investments, Inc. v. Brooks Woolen Co.*,<sup>213</sup> and by doing so, created a conflict of authority in the federal courts.

#### 1. The Plain Language of FIRREA Transfers No Jurisdiction to Assignees

Courts in the minority applied canons of statutory interpretation to analyze FIRREA and concluded that no subject matter jurisdiction existed in the action after the FDIC or RTC withdrew from the case. The *New Rock* court mapped out its "plain meaning" analysis of FIRREA, and considered the language of the statute, its legislative history, and the "atmosphere in which [it] was enacted."<sup>214</sup> The *Mill* court reasoned that the failure of the statute to mention assignees was significant and Congress clearly intended that only the FDIC should benefit from federal jurisdiction.<sup>215</sup> FIRREA lacked equivalent language indicating such intent for its assignees.<sup>216</sup>

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1991).

209. See *CIT*, 1997 U.S. Dist. LEXIS 12844, at \*23 ("[T]he parties need not litigate an entire controversy, only to discover after much time and expense that the basis for federal jurisdiction has eroded, and they must refight their battles in state court.").

210. *Id.* (citing *Freeport-McMoRan, Inc. v. K N Energy, Inc.*, 498 U.S. 426, 428 (1991)).

211. The Court of Appeals for the Second Circuit followed *Griffin* in *Four Star*, 178 F.3d at 100.

212. 101 F.3d 1492 (3d Cir. 1996).

213. 797 F. Supp. 49 (D. Me. 1992).

214. *New Rock*, 101 F.3d at 1498.

215. See *Mill*, 797 F. Supp. at 54.

216. See *id.* ("Although Congress might have given removal power to assignees or transferees from the FDIC to assure federal court application of *D'Oench, Duhme*, it



The *New Rock* court found little guidance in the jurisdictional language of FIRREA to decide whether assignees could remain in federal court.<sup>217</sup> The Third Circuit consulted the legislative history and noted three "obvious ways" that federal jurisdiction aided the RTC in fulfilling its statutory purpose to administer and dispose of thrift assets.<sup>218</sup> According to the court, the RTC enjoyed a federal forum and a uniform body of federal law on account of its (1) receivership functions, (2) the litigation of claims on behalf of the thrifts it controls and (3) its enforcement authority.<sup>219</sup> Applying that conclusion to the case before them, the Third Circuit determined that once the RTC succeeded in either returning a thrift to solvency or transferring its assets to willing purchasers, "the agency's role—and hence the logic of jurisdiction—no longer exist[ed]."<sup>220</sup> The court concluded that the purpose of the statute defining the RTC's role to manage and dispose of thrift assets supported the narrowest reading of the statute.<sup>221</sup> Jurisdiction existed only "where the RTC is a party but not where it *was* a party."<sup>222</sup>

The *New Rock* court commented that its reading was "consistent with general policies underlying federal jurisdiction . . . [,] the limited nature of federal jurisdiction and the goal of not interfering in the business of the states."<sup>223</sup> The *New Rock* court concluded that no independent basis for federal court jurisdiction existed.<sup>224</sup> Once the FDIC was no longer a party to the action, the once jurisdictionally sufficient case no longer involved a federal question, and thus became merely a suit between non-diverse parties based in state law.<sup>225</sup>

## 2. The Minority Rejection of the Time-of-Filing Rule

Instead of applying the time-of-filing rule, the *New Rock* majority applied 28 U.S.C. § 1367, the supplemental jurisdiction statute.<sup>226</sup> According to the court in *New Rock*, the time-of-filing rule applied primarily to cases removed to federal courts based on diversity of citizenship, and it functioned to prevent "manipulative behavior" in federal courts, such as amending pleadings to lower the amount in

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did not.").

217. See *New Rock*, 101 F.3d at 1498.

218. *Id.* at 1500.

219. See *id.* at 1501.

220. *Id.*

221. See *id.*

222. *Id.* at 1499. The court further stated that "[t]he RTC will presumably only be a party where it is engaged in active management and disposal of thrifts and thrift assets. The RTC will no longer be a party—and jurisdiction will no longer apply—once the RTC has managed a thrift and its assets have been disposed." *Id.* at 1501.

223. *Id.* at 1502.

224. See *id.* at 1501.

225. See *id.*

226. See *id.* at 1504-11.

controversy to avoid removal or changing parties to destroy diversity.<sup>227</sup> The court disapproved of the time-of-filing rule's "axiomatic" application in federal question cases.<sup>228</sup> Furthermore, according to the court, the FDIC's sale of the assets of the failed depository institution to a private party is a transaction at arms-length,<sup>229</sup> in good faith and in the ordinary course of business.<sup>230</sup> The court therefore did not apply a rule that primarily dealt with deterring a party's tactical efforts to avoid federal jurisdiction.<sup>231</sup>

As a result, the *New Rock* court rejected the time-of-filing rule and instead applied the supplemental jurisdiction statute.<sup>232</sup> It analogized the situation of law (where a single claim lost its federal jurisdiction by a substitution of parties) to § 1367(c)(3), the dismissal of the jurisdiction-conferring claim in a multiple claim action.<sup>233</sup> The court found its application of the supplemental jurisdiction statute within the permissible limits of Article III of the Constitution.<sup>234</sup> The court compared the constitutional propriety of the single transformed claim to dicta in the Supreme Court case of *Martinez v. Lamagno*.<sup>235</sup> There, the Court allowed judicial review in federal court although the United States was not a party to the litigation at the time of the appeal and the case had no basis for federal subject matter jurisdiction.<sup>236</sup> The Court reasoned that "there was a nonfrivolous federal question, certified by the local United States Attorney, when the case was removed to federal court. At that time, the United States was the defendant, and the action was thus under [federal court jurisdiction]." <sup>237</sup>

To justify invoking supplemental jurisdiction in the situation before it, although there were no multiple claims or multiple parties as defined under § 1367, the *New Rock* court argued that Congress intended to confer federal jurisdiction to its constitutional limits.<sup>238</sup> The court noted that the language of the statute mirrored Article III's reference to a "case or controversy."<sup>239</sup> The court claimed that § 1367's legislative history contained evidence that Congress sought to

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227. *Id.* at 1503 ("From the outset, the underlying concern of the time of filing rule was the risk that parties would deploy procedural tactics to manipulate federal jurisdiction.").

228. *Id.*

229. *See id.* at 1504.

230. *See* Black's Law Dictionary 109 (6th ed. 1990) (defining arms length transaction).

231. *See New Rock*, 101 F.3d at 1504.

232. *See id.* at 1505.

233. *See id.*

234. *See id.*

235. 515 U.S. 417, 435 (1995).

236. *See id.*

237. *Id.*

238. *See New Rock*, 101 F.3d at 1509.

239. *See id.*; *see also* U.S. Const. art. III, § 2 (describing scope of judicial power).

restore ancillary and pendent jurisdiction to its status before the Supreme Court decision in *Finley v. United States*,<sup>240</sup> to reflect the approach of *United Mine Workers of America v. Gibbs*.<sup>241</sup> The court expressed its belief that under *Gibbs*, supplemental jurisdiction extended to the constitutional limit, absent any action by Congress to restrict its exercise.<sup>242</sup> As such, the *New Rock* court rejected the time-of-filing rule and applied the supplemental jurisdiction statute.<sup>243</sup> Instead of remanding the case to the district court to apply § 1367, the court affirmed the lower court's jurisdiction and its order for summary judgment.<sup>244</sup>

The next part further examines the issue of whether federal jurisdiction exists after the FDIC transfers its assets to a third party and exits federal court litigation, leaving non-diverse parties who assert only state law claims. The next part explores additional case law dealing with the law of assignments, the time-of-filing rule and supplemental jurisdiction.

#### IV. ANALYSIS

This part examines the theories of the majority and minority courts discussed in Part III in greater depth to resolve whether private parties that purchase assets from the FDIC during pending federal court litigation may continue there after the FDIC is no longer a party to the case and only state law claims are at issue between non-diverse parties. It scrutinizes related case law dealing with assignment, the time-of-filing rule and the supplemental jurisdiction statute in order to determine the merits of adopting each individual approach.

First, this part analyzes the theory of assignment as it has been discussed in case law dealing specifically with the FDIC. The cases look to the common law of assignment and include jurisdiction as a "stick" in the bundle of rights purchased by assignees. Other cases refine this view and hold that jurisdiction is based on the FDIC's federal party status and therefore is non-transferable.<sup>245</sup> As a potential answer to these concerns about federal party status, a third approach to assignment is discussed. This approach relies upon the Supreme Court decision in *Vermont Agency of Natural Resources v. United States*,<sup>246</sup> where the Court used the theory of partial assignment

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240. 490 U.S. 545, 548 (1989); see *supra* notes 137-42 and accompanying text.

241. 383 U.S. 715 (1966); see *New Rock*, 101 F.3d at 1509.

242. See *New Rock*, 101 F.3d at 1509. The court described the "pre-*Finley*" understanding of the scope of supplemental jurisdiction as "where Congress has not spoken to the contrary or where we cannot find Congressional intent to the contrary, jurisdictional statutes give federal courts the power to exercise ancillary and pendent jurisdiction to the constitutional limit." *Id.* (quotations omitted).

243. See *id.* at 1511.

244. See *id.* at 1511-12.

245. See *infra* notes 280-82 and accompanying text.

246. 120 S. Ct. 1858 (2000).

to allow relators to bring a *qui tam* action on behalf of the United States.<sup>247</sup>

This part next assesses the time-of-filing rule as a mechanism to preclude later challenges to jurisdiction based on subsequent changes in parties or events. Last, the part discusses whether the supplemental jurisdiction statute allows private parties that purchase assets from the FDIC to litigate in federal court when the FDIC is no longer a party.

### A. Assignment

Courts espousing the majority position have used the assignment rationale to allow a wholesale transfer of federal jurisdiction from the FDIC to a private party.<sup>248</sup> Courts first applied the assignment analysis to extend the common law *D'Oench, Duhme* powers to transferees,<sup>249</sup> and then used it to allow private parties to avail themselves of the FIRREA six-year statute of limitations.<sup>250</sup>

#### 1. Assigning Federal Common Law Rights and Statutory Rights under FIRREA

Although assignment has been widely applied to allow private party purchasers to exercise *D'Oench, Duhme* common law powers, some courts have not shown the same willingness to extend to assignees the FDIC's procedural advantages, such as its statute of limitations. Case law dealing with the assignment of the FDIC's statute of limitations is more analogous to the issue of the FDIC's federal jurisdiction than *D'Oench, Duhme* since the statute of limitations and jurisdiction are both procedural and statutory features of the FDIC.

Under FIRREA, the statute of limitations on any action brought by the FDIC as conservator or receiver is the longer of either the six-year period beginning on the date the claim accrues, or the period applicable under state law.<sup>251</sup> The statute of limitations starts to run

247. See *id.* at 1863.

248. See, e.g., *FSLIC v. Griffin*, 935 F.2d 691, 696 (5th Cir. 1991) ("A transferee from the FSLIC, or FDIC, as successor of their interests, is still entitled to the protection of federal courts applying *D'Oench, Duhme*. . .").

249. See *supra* notes 91-99 and accompanying text.

250. See *infra* notes 251-73 and accompanying text.

251. 12 U.S.C. § 1821(d)(14) states in pertinent part:

(14) Statute of limitations for actions brought by conservator or receiver  
 (A) In general. Notwithstanding any provision of any contract, the applicable statute of limitations with regard to any action brought by the Corporation as conservator or receiver shall be  
 (i) in the case of any contract claim, the longer of  
 (I) the 6-year period beginning on the date the claim accrues;  
 or  
 (II) the period applicable under State law. . . .

12 U.S.C. § 1821(d)(14) (1994).

on the date the FDIC is appointed as conservator or receiver, or the date on which the cause of action accrues, whichever is later.<sup>252</sup>

A majority of federal and state courts have permitted assignment of the benefits of the FIRREA's six-year statute of limitations period to the FDIC's and RTC's assignees by relying on the same reasoning they used to extend common law *D'Oench, Duhme* powers to private entities.<sup>253</sup> To decide whether assignees could exercise the federal statute of limitations, courts looked either to federal common law or to state law to construe what rights pass through assignment from the FDIC to the private entity.<sup>254</sup> The Fifth Circuit in *FDIC v. Bledsoe*<sup>255</sup> relied on federal common law.<sup>256</sup> The court looked to principles of common law and *D'Oench, Duhme* and declared that "[a]n assignee stands in the shoes of his assignor."<sup>257</sup>

In addition, the statute of limitations, like common law *D'Oench, Duhme* powers, advanced the FDIC's goals of managing the assets of failed banks and protecting insured depositors while minimizing the cost to the insurance fund.<sup>258</sup> The court feared that the market for assets of failed banks would evaporate if the third party purchaser could not assert the FDIC's statute of limitations.<sup>259</sup> The FDIC would

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252. See Brian J. Woram, *FIRREA's Statutes of Limitations: Their Availability to Purchasers from the FDIC*, 110 Banking L.J. 292, 294 (1993).

253. See *UMLIC-Nine Corp. v. Lipan Springs Dev. Corp.*, 168 F.3d 1173, 1177 n.3 (10th Cir. 1999) (extending statute of limitations to assignees); *Cadle Co. v. 1007 Joint Venture*, 82 F.3d 102, 105 (5th Cir. 1996) (applying FIRREA statute of limitations to notes in default before they were acquired by the FDIC or while owned by the FDIC); *United States v. Thornburg*, 82 F.3d 886, 889-92 (9th Cir. 1996) (applying common law of assignments); *FDIC v. Bledsoe*, 989 F.2d 805, 811 (5th Cir. 1993) (relying on common law and *D'Oench, Duhme*); see also *Tivoli Ventures, Inc. v. Tallman*, 870 P.2d 1244, 1246 (Colo. 1994) (extending FIRREA statute of limitations to private assignees); *Cadle Co. v. Lewis*, 864 P.2d 718, 724 (Kan. 1993) (relying on common law and extension of *D'Oench, Duhme*); *Central States Resources v. First Nat'l Bank*, 501 N.W.2d 271, 278 (Neb. 1993) (reasoning that assignee who stands in shoes of FDIC "obtains the right, title, and interest that the assignor had at the time of assignment"); *SMS Fin. v. Ragland*, 918 P.2d 400, 403 (Okla. 1995) (same); *Jackson v. Thweatt*, 883 S.W.2d 171, 178 (Tex. 1994) (same). No circuit court or state supreme court has held that the six-year statute of limitations does not apply to assignees. *But see* *Bleckley Capital Ltd. Partnership v. Di Geronimo*, 184 F.3d 52, 57 (1st Cir. 1999) (stating hesitance to read statute as covering assignees, but, applying state law on alternate grounds); *Federal Debt Management v. Weatherly*, 842 S.W.2d 774, 778 (Tex. Ct. App. 1992) (finding statute of limitations was not a "right" inherited by assignee).

254. See *National Enters., Inc. v. Barnes*, 201 F.3d 331, 334 (4th Cir. 2000) (applying South Carolina law); *Federal Fin. Co. v. Hall*, 108 F.3d 46, 50 (4th Cir. 1997) (applying Virginia law); *Remington Invest., Inc. v. Kadenacy*, 930 F. Supp. 446, 448 (D. Cal. 1996) (holding that California law allows FDIC's 6-year statute of limitations to pass to assignees).

255. 989 F.2d 805 (5th Cir. 1993).

256. See *id.* at 810.

257. *Id.* (emphasis in original).

258. See Woram, *supra* note 252, at 301.

259. See *Bledsoe*, 989 F.2d at 811 (citing *Fall v. Keasler*, No. C 90 20643 SW, 1991 U.S. Dist. LEXIS 18771, at \*8 (Dec. 18, 1991 N.D. Cal. 1991)).

be unable to sell notes that had expired, or would be about to expire, under the shorter state statute of limitations.<sup>260</sup> Asset recovery would depend in large part on the FDIC's own litigation efforts.<sup>261</sup> Such an outcome would stymie Congress' desire for the FDIC to "rid the federal system of failed bank assets."<sup>262</sup>

As in *Bledsoe*, the court in *Wamco III, Ltd. v. First Piedmont Mortgage Corp.*<sup>263</sup> relied on the common law of assignments, but reached a contrary result. The *Wamco* court concluded that assignees should not receive the benefit of the longer statute of limitations established by § 1821(d)(14). According to the court, "unless a contrary intention is manifest or inferable, an assignment ordinarily carries with it all rights, remedies and benefits which are incidental to the thing assigned, *except those which are personal to the assignor and for his benefit only.*"<sup>264</sup> The court concluded that because Congress clearly made the six-year statute of limitations in FIRREA applicable only to actions brought by the RTC in its status as receiver, the RTC's statute of limitations was non-assignable.<sup>265</sup>

Following the Supreme Court decisions in *O'Melveny & Myers v. FDIC*<sup>266</sup> and *Atherton v. FDIC*<sup>267</sup> holding that new federal common law should not be created where there exists a comprehensive and detailed statutory scheme like FIRREA, lower federal courts stopped applying federal common law when deciding whether an assignee of the FDIC may invoke the statute of limitations applicable to the FDIC under FIRREA.<sup>268</sup> For example, the Fourth Circuit declined to

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260. See Boteler, *supra* note 6, at 1170 ("If the FDIC can only transfer the rights incidental to the notes and not extend the six year limitations period, then the FDIC will have to pursue and litigate the recovery of all those assets and notes for which the state statute of limitations has already run.").

261. See *id.*

262. *Bledsoe*, 989 F.2d at 811 (quoting *Fall v. Keasler*, 1991 U.S. Dist. LEXIS 18771, at \*8).

263. 856 F. Supp. 1076 (E.D. Va. 1994).

264. *Id.* at 1086 (emphasis in original) (internal quotations omitted).

265. See *id.*

266. 512 U.S. 79 (1994).

267. 519 U.S. 213 (1997).

268. See *infra* notes 269-73 and accompanying text. In *O'Melveny & Myers*, the FDIC tried to persuade the Court to create federal common law allowing the FDIC to avoid imputation of knowledge of a failed savings and loan directors' breach of fiduciary duty and legal malpractice. *O'Melveny & Myers*, 512 U.S. at 80. The Court, in accord with its holding in *Erie*, refused to create new common law because *Erie* clearly held that federal common law does not exist. See *Erie R.R. Co. v. Tompkins*, 304 U.S. 64, 78 (1938). In addition, the Court refused to preempt state law by reading into the statutory provisions of FIRREA a rule allowing the FDIC to displace state law, thus avoiding imputation of knowledge of the directors' malfeasance upon the failed bank and its receiver, the FDIC. See *O'Melveny & Myers*, 512 U.S. at 85. The Court reasoned that because a "comprehensive and detailed" statutory scheme already existed, the rule of decision concerning matters that Congress did not address would presumably be derived from state law, and not some court-created supplement to federal regulation. *Id.*

In *Atherton*, 519 U.S. 213 (1997), the Supreme Court again refused to create federal

extend the benefit of the longer statute of limitations to assignees, although it acknowledged that it extended *D'Oench, Duhme* and § 1823(e) to assignees.<sup>269</sup> Citing *O'Melveny & Myers* and *Atherton* as controlling law, the Fourth Circuit stated that it lacked a compelling reason to create a new rule of federal common law.<sup>270</sup> The application of state law did not conflict with a federal interest or policy, which was a necessary element to justify the creation of federal common law.<sup>271</sup> The Fourth Circuit concluded that no conflict existed because the FDIC's assignees were "one step further removed from the primary conduct of the United States than the government agency receiver whose role the *O'Melveny & Myers* court found to be too attenuated" to create federal common law.<sup>272</sup> Consequently, the court deferred to Congress' ability to enact legislation and elected to "remain mere observers."<sup>273</sup> In conclusion, *O'Melveny & Myers* and *Atherton* make it unlikely that support for the extension of jurisdiction to assignees can be based on an extension of *D'Oench* and federal common law. An alternate approach based on theories of assignment and jurisdiction follows.

## 2. Refining the Assignment Analysis

Several district courts have declined to hold that the FDIC's federal jurisdictional statute applies to a private party who has purchased assets from the FDIC.<sup>274</sup> In a series of cases that dealt with whether the assignment of delinquent notes included the assignment of the right to file suit in federal court under the FDIC's jurisdictional statute,<sup>275</sup> these courts have applied the common law rule that the assignee acquires all of the rights and liabilities of the assignor.<sup>276</sup>

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common law to determine the proper legal standard of care in an action brought by the RTC against the directors of a failed depository institution. *Id.* at 218. Following its previous holdings establishing the preconditions necessary before it can exercise its common-law-making powers, the Court first examined whether there existed any significant conflict between a federal policy or interest and the application of state law standards. *See id.* at 219. The Court found no significant conflict between a federal policy or interest and the application of state law standards that would allow them to create a rule of federal common law. *See id.*

269. *See* Federal Fin. Co. v. Hall, 108 F.3d 46, 49 (4th Cir. 1997).

270. *See id.*

271. *See id.*

272. *Id.* (internal quotations omitted).

273. *Id.* at 50.

274. *See infra* note 275.

275. *See* RTC Commercial Assets Trust 1995-NP3-1 v. Phoenix Bond Indem. Co., 943 F. Supp. 962, 963 (N.D. Ill. 1996) (bringing suit under FIRREA 12 U.S.C. § 1825(b) to void tax lien due to status as assignee of the RTC); S1 IL304 Ltd. Liab. Co. v. ANB Cust. for LG *ex rel* Hynes, 950 F. Supp. 242, 246 (N.D. Ill. 1996) (same); RTC Commercial Loan Trust 1995-NP1A v. Winthrop Management, 923 F. Supp. 83, 88 (E.D. Va. 1996) (rejecting plaintiff claims that the right to sue under § 1821(d)(17)(A) of FIRREA included rights assigned from RTC).

276. *See, e.g., Phoenix Bond*, 943 F. Supp. at 965 ("Typically an assignee acquires

These courts relied on an exception to the general rule of assignments, which states that rights that are personal to the assignor cannot be assigned.<sup>277</sup> According to these courts, the FDIC's federal agency jurisdiction is a personal right that cannot be assigned.<sup>278</sup> These courts are of the opinion that an assignee should not succeed to the FDIC's subject matter jurisdiction absent a Congressional grant in § 1819(b).<sup>279</sup>

Similarly, a Virginia district court opinion distinguished jurisdiction from the ability to assert common law *D'Oench, Duhme* on the basis of "status-versus-rights."<sup>280</sup> The court argued that § 1441(a), the RTC's equivalent jurisdictional statute, was not a right, and instead, it merely conferred federal jurisdiction.<sup>281</sup> The RTC could neither alienate its "status" as a federal party nor could it "deputize a private party with the full powers of RTC."<sup>282</sup>

A Massachusetts district court agreed that the purchase of notes from the FDIC did not entitle the purchaser to invoke the FDIC's removal statute.<sup>283</sup> According to the court, removal to federal court was merely a "procedural dimension" of the FDIC's federal party status.<sup>284</sup> Similarly, in an opinion from the Eastern District of Louisiana, the court held that the purchase of a mortgage from the RTC did not make the plaintiff an agent of the RTC for the purposes of federal question jurisdiction.<sup>285</sup> The defendant, therefore, lacked the ability to remove the case from Louisiana state court because the claim did not arise under federal law and no diversity existed.<sup>286</sup>

These minority courts challenge the ability of the FDIC to assign federal jurisdiction to private party purchasers because they classify the FDIC's jurisdiction, based on its status as a federal party, as a personal right that cannot be transferred under the common law of

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all the assignor's rights and liabilities in the assignment.").

277. See *id.*; *Winthrop Management*, 923 F. Supp. at 88.

278. See *Phoenix Bond*, 943 F. Supp. at 965; *Winthrop Management*, 923 F. Supp. at 88.

279. See *Phoenix Bond*, 943 F. Supp. at 965. The *Phoenix Bond* Court wrote: Extending certain defenses, and even statutory limitations periods, is decidedly different than extending this court's original jurisdiction. Congress explicitly stated that federal subject matter jurisdiction would exist when the RTC is a party to the lawsuit. It could have identified RTC or its assigns, but did not. The right to sue in federal court is a benefit that is generally personal unless a statute dictates otherwise.

*Id.*

280. *Winthrop Management*, 923 F. Supp. at 87.

281. See *id.* at 88.

282. *Id.* at 87.

283. See *Brae Asset Fund, L.P. v. Dion*, 929 F. Supp. 29, 31 (D. Mass. 1996).

284. *Id.*

285. See *Vanderbilt Mortgage & Fin. Co. v. Acceptance Ins. Co.*, No. 96-0155, 1996 U.S. Dist. LEXIS 2416 at \*4 (E.D. La. Feb. 27, 1996).

286. See *id.* at \*5.



assignments.<sup>287</sup> Minority courts also have argued that jurisdiction is a procedural feature and not a right.<sup>288</sup> A recent Supreme Court decision may nevertheless acknowledge the ability of a federal party to assign its status for the purposes of jurisdiction.<sup>289</sup>

In *Vermont Agency of Natural Resources v. United States*, the Supreme Court adopted an assignment approach to allow private citizens who bring *qui tam* actions to meet the standing threshold of Article III of the Constitution.<sup>290</sup> *Qui tam* is an abbreviation of a Latin phrase that is translated in its entirety as, "[w]ho sues on behalf of the King as well as for himself."<sup>291</sup> To establish standing and meet the "case or controversy" requirement of Article III of the Constitution, a plaintiff must show an "injury-in-fact" to a concrete degree, establish causation between the alleged conduct of the defendant and the injury-in-fact, and demonstrate that the relief requested will redress the claimed injury.<sup>292</sup> The False Claims Act enables a person who possesses knowledge of fraud perpetrated against the Federal Government to bring suit both on this person's own behalf and on behalf of the United States.<sup>293</sup> Article III requires that the injury-in-fact be suffered by the complaining party, but when a person sues as a *qui tam* relator, it is the United States who suffered the alleged injury.<sup>294</sup> The Court held that private citizens who bring a claim under the False Claims Act could satisfy the Constitutional standing requirement because through the Act, Congress makes a partial assignment of the government's claim.<sup>295</sup> The Court declared,

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287. See *supra* notes 280-82 and accompanying text.

288. See *supra* notes 283-84 and accompanying text.

289. See *Vermont Agency of Natural Resources v. United States ex rel Stevens*, 120 S. Ct. 1858 (2000).

290. See *id.* at 1863; see also *United States ex rel Kelly v. Boeing Co.*, 9 F.3d 743, 748 (9th Cir. 1993) (holding that the federal government's claims are assigned through the false claims Act); *United States ex rel Waris v. Staff Builders, Inc.*, No. 96-1969, 1999 U.S. Dist. LEXIS 2998 at \*10 (11th Cir. Mar. 4, 1999) (adopting assignment theory); *United States ex rel Chandler v. Hektoen Inst. for Med. Research*, 35 F. Supp. 2d 1078, 1081 (N.D. Ill. 1999) (same); *United States ex rel Yankton Sioux Tribe v. Gambler's Supply, Inc.*, 925 F. Supp. 658, 668 n.12 (D.S.D. 1996) (recognizing assignment as possible rationale); Thomas R. Lee, Comment, *The Standing of Qui Tam Relators Under the False Claims Act*, 57 U. Chi. L. Rev. 543, 565-70 (1990) (advocating the adoption of an assignment theory to allow a *qui tam* plaintiff to satisfy constitutional standing requirements).

291. Black's Law Dictionary 1251 (6th ed. 1990).

292. *Vermont Agency of Natural Resources*, 120 S. Ct. at 1861.

293. See James Y. Ho, Note, *State Sovereign Immunity and The False Claims Act: Respecting the Limitations Created by the Eleventh Amendment Upon the Federal Courts*, 68 Fordham L. Rev. 189, 189 (1999).

294. See *Vermont Agency of Natural Resources*, 120 S. Ct. at 1862.

295. See *id.* at 1863. The assignment is partial because under the False Claims Act the government may intervene in the action within 60 days of the relator's delivery of the complaint, or may do so afterwards by a good cause showing. See *id.* at 1861. The government keeps 70%-85% of the proceeds of the action, depending on whether or not it has intervened. See *id.*

"the assignee of a claim has standing to assert the injury in fact suffered by the assignor."<sup>296</sup> When the government has established the requisite injury-in-fact, causation and redressability, the relator becomes eligible to sue in federal court by way of assignment.<sup>297</sup>

The assignment approach articulated by the Supreme Court in *Vermont Agency of Natural Resources* refutes the idea that federal party status or agency status cannot be assigned.<sup>298</sup> If a private party can succeed to the federal government's injury-in-fact by way of assignment, a party may likewise succeed to a federal agency's federal party status for Article III purposes. But unlike the False Claims Act, where Congress explicitly conferred upon private parties the right to bring an action on behalf of the United States, a similar right of private parties to bring suit under FIRREA is absent.<sup>299</sup>

The next part discusses the time-of-filing rule. The part highlights the rule's application by courts to interpret the effect of the administrative claims procedure under FIRREA on the jurisdiction of federal and state courts.

### B. Time of Filing

Courts when interpreting other provisions of FIRREA have applied the time-of-filing rule. Courts have applied the time-of-filing rule and interpreted FIRREA to uphold the existence of subject matter jurisdiction in federal and state courts against FDIC and RTC assertions of exclusive jurisdiction in the administrative claims process. State courts used the rule to uphold concurrent jurisdiction over pending claims brought before the appointment of the RTC and FDIC as receivers despite RTC and FDIC assertions that the federal courts retain exclusive jurisdiction.<sup>300</sup> Likewise, federal courts used

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296. *Id.* One court characterized this notion by stating, "the qui tam plaintiff effectively stands in the shoes of the government." *United States ex rel Kelly v. Boeing Co.*, 9 F.3d 743, 748 (9th Cir. 1993).

297. See *Vermont Agency of Natural Resources*, 120 S. Ct. at 1863.

298. See *supra* notes 276-82 and accompanying text.

299. See *supra* notes 214-16 and accompanying text.

300. See, e.g., *RTC v. Foust*, 869 P.2d 183, 193 (Ariz. 1993) (rejecting exclusive federal court jurisdiction and noting that "Congress, in enacting FIRREA, could have overridden the time of filing rule and divested all other courts of jurisdiction"); *Robbins v. Foothill Nissan*, 28 Cal. 2d 190, 198 (Cal. Ct. App. 1994) (rejecting an automatic rule to divest state court of jurisdiction after the FDIC became receiver when claim against depository institution began in state court before appointment); *Berke v. RTC*, 483 N.W.2d 712, 715 (Minn. 1992) ("Measuring jurisdiction as of the time of filing is consistent with traditional authorities."); *RTC v. Binford*, 844 P.2d 810, 816 (N.M. 1992) (holding that state court retained the subject matter jurisdiction that vested when counterclaims were originally filed, despite subsequent RTC appointment as receiver).

For a critical look at the RTC's attempts to establish exclusive federal subject matter jurisdiction in claims brought against the RTC in the receivership capacity, see generally Jeffrey S. Rosenblum, *The RTC's Quest for Exclusive Federal Court Jurisdiction Under FIRREA*, 24 Mem. St. U. L. Rev. 725 (1994). Rosenblum finds no

the time-of-filing rule as a ground to keep jurisdiction over claims brought against the depository institution before it went into receivership.<sup>301</sup> These cases illustrate the belief held by many courts that the application of the time-of-filing rule is consistent with FIRREA.

The Supreme Court has declined to apply the time-of-filing rule only in exceptional circumstances and has done so in the interest of factors such as the finality of a judgment.<sup>302</sup> It is, therefore, unlikely that they will decline to apply the time-of-filing rule when the FDIC sells assets to a private party and only non-diverse parties and state law claims remain in the action, unless they do so on a case-by-case basis in the interests of preserving a final judgment.

The legal controversy addressed here is readily distinguished from those exceptional circumstances. In *Caterpillar* and *Newman-Green*, jurisdiction did not exist at the outset of the case and later the defect was cured.<sup>303</sup> In both cases, the district court had already entered judgment.<sup>304</sup> By contrast, under 12 U.S.C. § 1819(b)(2)(A), the FDIC's presence in the lawsuit confers subject matter jurisdiction at the outset of litigation, or whenever the FDIC joins the action.<sup>305</sup> Arguably, a jurisdictional defect is only created after the FDIC has transferred its assets to a non-diverse party.

### C. Supplemental Jurisdiction

As discussed in Part III, the minority courts declined to apply the time-of-filing rule to determine whether subject matter jurisdiction

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explicit statutory grant of exclusive jurisdiction in FIRREA. *See id.* at 728. His analysis of the statutory provisions for the administrative claims procedure, judicial review of administrative claims, 90 day stay of actions ongoing in court when the RTC is appointed as receiver, and removal, all support concurrent jurisdiction. *See id.* at 728-35. Rosenblum notes, however, that in light of the liberal removal authority granted by FIRREA, the more confounding question about exclusive jurisdiction is "why anyone really cares." *Id.* at 738.

301. *See, e.g.,* *Holmes Fin. Assocs. v. RTC*, 33 F.3d 561, 565 (6th Cir. 1994) (stating in dicta, "[a]lthough we have no doubts that Congress may override this 'time of filing' rule if it so chooses, . . . we believe that there is an even greater need for clear and affirmative Congressional action when it would do so."); *Marquis v. FDIC*, 965 F.2d 1148, 1155 (1st Cir. 1992) (holding that FIRREA does not require a federal court's automatic dismissal of claims brought against institution before FDIC was appointed receiver); *Praxis Properties v. Colonial Sav. Bank*, 947 F.2d 49, 63 n.14 (3d Cir. 1991) (affirming determination of jurisdiction at the time of filing so that the federal court is not divested of jurisdiction when the RTC becomes receiver during litigation). *But see* *New Maine Nat'l Bank v. Reef*, 765 F. Supp. 763, 765-66 (D. Me. 1991) (interpreting FIRREA provision to give courts discretion to continue jurisdiction of ongoing claim against depository institution after FDIC becomes receiver).

302. *See supra* notes 173-85 and accompanying text.

303. *See supra* notes 173-85 and accompanying text.

304. *See supra* notes 173-85 and accompanying text.

305. *See supra* note 186 and accompanying text.

still remained after the FDIC sold failed bank assets to a private party and then exited the litigation.<sup>306</sup> Faced with only non-diverse parties and claims based in state law, the minority instead held that the discretionary approach of the supplemental jurisdiction statute was appropriate.<sup>307</sup> In cases outside the context of private party purchasers and the FDIC, other courts adopted a similar approach and applied the supplemental jurisdiction statute to decide cases where events after the time of filing threatened to unsettle federal court jurisdiction.<sup>308</sup> Some courts, such as the Fourth Circuit, even claimed that the supplemental jurisdiction statute abrogated the time-of-filing rule.<sup>309</sup>

The Fourth Circuit, in *Shanaghan v. Cahill*,<sup>310</sup> held that § 1367 displaced the time-of-filing analysis of *St. Paul Mercury Indemnity Co. v. Red Cab Co.*<sup>311</sup> The court reviewed a district court ruling that dismissed a case for lack of jurisdiction when the plaintiff's aggregated claims in a diversity action fell below the amount in controversy.<sup>312</sup> The Fourth Circuit reversed and remanded, instructing the district court to apply the supplemental jurisdiction statute.<sup>313</sup> The court reasoned that after dismissal of one of the aggregate claims, the amount in controversy could not be met, and as a result, "the jurisdictional basis of the action fade[d] away."<sup>314</sup> Using § 1367(c) the lower court could exercise its discretion whether to keep or dismiss the remaining claims.<sup>315</sup>

The court rejected the time-of-filing rule as overbroad and contrary to Congress' "emphatic preference for the *Gibbs* approach,"<sup>316</sup> which is a "discretionary determination" informed by "federal policy, comity, and considerations of judicial economy."<sup>317</sup> The court then considered the virtues of discretion over the vices of a mechanical rule.<sup>318</sup> The court found both a "rigid rule of retention" and a "rigid rule requiring dismissal" equally undesirable because retention would flood federal courts with trivial claims and dismissal would be

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306. See discussion *supra* Part III.B.1.

307. See discussion *supra* Part III.B.2.

308. See *Stevenson v. Severs*, 158 F.3d 1332, 1334 (D.C. Cir. 1998) (applying subject matter jurisdiction when recovery sought by plaintiff fell below amount in controversy); cf. *Bailey v. Wal-Mart Stores, Inc.*, 981 F. Supp. 1415, 1416 (N.D. Ala. 1997) (holding that the time-of-filing rule of *St. Paul Mercury Indemnity Co.* was overruled by the 1988 version of 28 U.S.C. § 1447(c)); *Goodman v. Wal-Mart Stores, Inc.* 981 F. Supp. 1083, 1084 (M.D. Tenn. 1997) (same).

309. See *Shanaghan v. Cahill*, 58 F.3d 106 (4th Cir. 1995).

310. 58 F.3d 106.

311. See *id.* at 111.

312. See *id.* at 109.

313. See *id.*

314. *Id.* at 110.

315. See *id.*

316. *Id.* at 111.

317. *Id.* at 110.

318. See *id.*

unjust.<sup>319</sup> The court endorsed a discretionary rule to balance those extremes.<sup>320</sup> The "contemporary congressional view of federal jurisdiction" embraced the notion of courts balancing convenience, fairness to both parties and the interests of judicial economy.<sup>321</sup> The court argued that Congress surely had little desire that a mechanical approach to jurisdiction, of which the time-of-filing rule is an example, survive the enactment of § 1367.<sup>322</sup>

The application of § 1367(c) to aggregation cases such as *Shanaghan* is arguably inappropriate<sup>323</sup> because "no single claim by itself carried plaintiff into federal court."<sup>324</sup> Section 1367(a) requires first that the court possess jurisdiction over an original claim.<sup>325</sup> Supplemental jurisdiction then extends to additional claims or parties that derive from the same nucleus of operative fact as the original claim.<sup>326</sup> In *Shanaghan* there was only one claim over which the federal court had subject matter jurisdiction because the aggregated claims were considered one claim for the purposes of subject matter jurisdiction.<sup>327</sup>

As part of the Federal Judicial Code Revision Project there is a proposed amendment to § 1367. The Reporter's note to Tentative Draft 2 of the Federal Judicial Code Revision Project cites the erroneous *Shanaghan* decision as part of the impetus for a new § 1367.<sup>328</sup> The proposed new version of § 1367 includes a definitional section that distinguishes a supplemental claim from a claim that confers original jurisdiction, known as a "freestanding" claim.<sup>329</sup>

Likewise, § 1367 was improperly applied by the *New Rock* court. Judge McKee authored a dissenting opinion in *New Rock* and echoed the critics of the *Shanaghan* decision when he noted that under the facts of *New Rock*, § 1367(a)'s requirements for supplemental jurisdiction were clearly lacking.<sup>330</sup> According to McKee, the *New Rock* court first misinterpreted Congress' intent in the enactment of

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319. *Id.* at 111.

320. *See id.* at 112 ("Justice is better served by a jurisdictional rule that includes some measure of discretion for the district court.").

321. *Id.* at 111.

322. *See id.*

323. *See* Amanda Dalton, Note, *Shanaghan v. Cahill: Supplementing Supplemental Jurisdiction*, 1996 BYU L. Rev. 281, 290 (arguing that each of the individual claims aggregated to exceed the amount in controversy threshold are not supplemental claims under § 1367(a)).

324. *Shanaghan*, 58 F.3d at 110.

325. *See* 28 U.S.C. § 1367(a) (1994).

326. *See id.*

327. *See supra* note 323 and accompanying text.

328. *See* ALI, Federal Judicial Code Revision Project 76-77 (T.D. 2) (1998).

329. New § 1367, as proposed by Tentative Draft No. 1 contains a definition that states in pertinent part: "a freestanding claim is any claim for relief that is within the original jurisdiction of the district courts independently of the jurisdiction conferred by this section. . . ." *Id.* at 155.

330. *See New Rock Asset Partners v. Preferred Entity Advancements, Inc.* 101 F.3d 1492, 1512 (3rd. Cir. 1996) (McKee, J., dissenting).

the supplemental jurisdiction statute.<sup>331</sup> The *New Rock* court misapplied § 1367(c) because the private party's claim was not an independent claim with supplemental jurisdiction status separate from the RTC's claim.<sup>332</sup> The RTC was no longer a party to the action after it sold the assets under litigation to the private party.<sup>333</sup> Jurisdiction over the remaining claim was not supplemental. Judge McKee noted that the *New Rock* opinion was further distorted because it "rel[ies] upon the very 'Time of Filing' rule that it reject[s] in the first instance."<sup>334</sup> For the court in *New Rock*, the proper removal by the FDIC at the time of filing conferred original jurisdiction for supplemental jurisdiction purposes but could not prevent the divestment of the FDIC assignee under FIRREA.<sup>335</sup> The disputed claim in *New Rock* failed to fall under the supplemental jurisdiction statute because the claim of the private party was not an individual claim separate from the RTC's jurisdiction-conferring claim.<sup>336</sup> Furthermore, the Third Circuit's decision in *New Rock* to make the exercise of jurisdiction discretionary is contrary to its finding that once the RTC was no longer a party to the case subject matter jurisdiction based on the RTC's federal party status in FIRREA did not survive.<sup>337</sup>

## V. ARGUMENT

This part illustrates the ways in which the time-of-filing rule currently offers the most satisfactory method for courts to exercise federal jurisdiction after the transfer of assets from the FDIC to a private party takes place. This Note suggests as an alternative solution that Congress amend FIRREA and confer federal jurisdiction on these private party purchasers as assignees of the FDIC to guarantee them the benefits of federal court jurisdiction.

The issue of subject matter jurisdiction should not be considered solely with regard to the case law that extends the FDIC's common law *D'Oench, Duhme* powers to assignees. The Supreme Court has already expressed its disapproval of the creation of federal common law.<sup>338</sup> In response, the FDIC has also curtailed its use of common law

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331. See *id.* at 1513-14 ("I do not think that the Congress intended to allow the exercise of federal jurisdiction to resolve a uniquely state claim where, as here, the federal court concludes that it has no original federal jurisdiction.").

332. See *id.* at 1515 n.2 ("[T]he dismissal of the RTC did not cause the federal claims to 'morph' into state claims.").

333. See *id.* at 1494.

334. *Id.* at 1514.

335. See *id.* McKee surmised, "[w]e are confronted with an error of law arising from what I believe is an erroneous application of a legal principle occasioned by an incorrect reading of the supplemental jurisdiction statute." *Id.*

336. Cf. *Wolde-Meskel v. Vocational Instruction Project Community Serv. Inc.*, 166 F.3d 59, 65 (2d Cir. 1999) (holding that state law claims aggregated together are original and individually are not supplemental for the purposes of § 1367).

337. See *supra* note 334 and accompanying text.

338. See *supra* notes 266-73 and accompanying text.

*D'Oench, Duhme*, and is relying instead on its statutory powers in FIRREA.<sup>339</sup> Cases discussed in Part III.A. properly distinguished the FDIC's federal party status from the rights of assignees to exercise *D'Oench, Duhme* common law because the FDIC's federal jurisdiction is not only the result of a Congressional grant, it is based upon the FDIC's status as an agency of the United States.<sup>340</sup>

Although the statute of limitations is a procedural rule, and therefore more analogous to jurisdiction than the *D'Oench, Duhme* doctrine, the statute of limitations is still an affirmative defense.<sup>341</sup> By contrast, parties have no power to consent to a waiver of subject matter jurisdiction.<sup>342</sup> The court may examine subject matter jurisdiction on its own motion, at any time during litigation.<sup>343</sup> The Federal Rule of Civil Procedure 12(h)(3) recognizes the constitutional importance of a federal court's subject matter jurisdiction by granting the court the authority to do so.

The Supreme Court's decision in *Vermont Agency of Natural Resources* suggests that a federal party's status may be assigned to a private party for the purpose of federal court subject matter jurisdiction.<sup>344</sup> However, while Congress clearly referred to private parties in the False Claims Act, § 1819(b)(2)(A) lacks any language about private parties.<sup>345</sup> The minority courts that have applied the

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339. See Statement of Policy, *supra* note 88. After the Supreme Court's decisions in *O'Melveny & Myers* and *Atherton* brought the expansion of federal common law to a halt, the FDIC issued a statement of policy containing guidelines for the agency's use of the common law *D'Oench, Duhme* doctrine. See, e.g., Galves, *Might Does Not Make Right*, *supra* note 6, at 1386-90 (arguing that the FDIC's internal guidelines should not prevent efforts to reform *D'Oench, Duhme*). This effort was surely an attempt to avoid further judicial erosion of the agency's superpower, see Barry Stuart Zisman, Banks and Thrifts: Government Enforcement and Receivership § 25.02[5] at 25-32 (1991), which the FDIC has called "among the most important, long-standing, and powerful protections afforded the FDIC." Statement of Policy, *supra* note 88. It acknowledged that, "overly aggressive application of the specific requirement of these legal doctrines could lead to inequitable and inconsistent results in particular cases." *Id.* at 5986. The FDIC announced that it would only apply § 1823(e) to "claims that relate to agreements or arrangements entered into after the effective date of FIRREA." *Id.* at 5985. Agreements entered into prior to the effective date of FIRREA would fall under pre-FIRREA § 1823(e) and the *D'Oench, Duhme* doctrine. See *id.* The guidelines however, will not curtail third party entities from asserting the *D'Oench, Duhme* doctrine when litigating post-FIRREA agreements. See Bock, *supra* note 60, at 986. Uncertainty still remains around the fate of the *D'Oench, Duhme* doctrine especially now that its fate may be in the hands of private parties.

340. See *supra* notes 275-286 and accompanying text.

341. Cf. Woram, *supra* note 252, at 306 ("[S]tatutes of limitation are shields of defense. . .").

342. See Chemerinsky, *supra* note 114, § 5.1 at 259.

343. Fed. R. Civ. P. 12(h)(3). The examination of subject matter jurisdiction is one of the few matters a court may consider on its own motion. See Chemerinsky, *supra* note 114, § 5.1 at 260.

344. See *supra* notes 290-97 and accompanying text.

345. See *supra* note 215 and accompanying text.

supplemental jurisdiction statute have done so mistakenly, exceeding the bounds of Congressional intent. The supplemental jurisdiction statute deals only with civil actions that consist of multiple claims.<sup>346</sup> The discretionary factors of § 1367(c) only arise when a court is deciding whether to decline jurisdiction on a supplemental claim.<sup>347</sup>

Congress would likely need to enact legislation to allow courts to apply the discretionary *Gibbs-Cohill* factors of § 1367(c) to determine whether to exercise jurisdiction after the FDIC transfers assets of a failed financial institution to a private party and leaves non-diverse parties asserting state law claims. Enacting a discretionary rule would permit district court judges to assess the efficiency, economy and fairness of a remand or possibly a dismissal on a case-by-case basis. However, a discretionary rule may present more risk to the private parties that purchase assets from the FDIC because the status of pending federal court litigation over these assets becomes uncertain. The market for these questionable assets could shrink as a result and lead to less of a recovery on these assets for the insurance fund.<sup>348</sup>

The time-of-filing rule offers a satisfactory solution to the issue of federal jurisdiction after the FDIC is no longer a party to pending litigation following a transfer of assets to a third party. Under the time-of-filing rule, the court's subject matter jurisdiction is settled according to § 1819(b)(2)(A) of FIRREA, by the presence of the FDIC as a party to the case.<sup>349</sup> The time-of-filing rule was created as a bright line rule to encourage "normal business transactions" during litigation.<sup>350</sup> This asset sale to private parties is a regular part of the FDIC's efforts in its capacity as a receiver, conservator or insurer to maximize the return to a failed bank's creditors and minimize expenditures out of the insurance fund and the pockets of taxpayers.<sup>351</sup> Congress sanctions these policy goals in FIRREA.<sup>352</sup>

The minority courts found the time-of-filing rule inapplicable because they maintained that the rule's only purpose was to deter manipulative behavior by parties.<sup>353</sup> When the FDIC transfers its assets to a private party during the course of ongoing litigation, application of the time-of-filing rule may prevent manipulative

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346. See *supra* notes 323-29 and accompanying text.

347. See *supra* notes 308-37 and accompanying text.

348. Cf. Woram, *supra* note 252, at 304 ("Once an asset might lose the protection in a purchaser's hands, its value declines in the FDIC's hands.").

349. See, e.g., *CIT, Inc. v. 170 Willow St. Assocs.*, 93 Civ. 1201 (CSH), 1997 U.S. Dist. LEXIS 12844 at \*14 (S.D.N.Y. Aug. 26, 1997) (citing cases that apply time-of-filing rule).

350. *Freeport-McMoRan, Inc. v. K N Energy, Inc.*, 498 U.S. 426, 428-29 (1991) (*per curiam*).

351. See *supra* notes 54-86 and accompanying text.

352. See Woram, *supra* note 252, at 301.

353. But see *CIT*, 1997 U.S. Dist. LEXIS 12844 at \*22-\*23 (declaring "the need to prevent improper manipulation of federal jurisdiction is not the only policy rationale underlying this rule").



behavior on the part of the debtor whose motive for challenging jurisdiction could be to win a dismissal and avoid having the case judged on the merits.<sup>354</sup>

Rather than simply relying on courts to uniformly apply the time-of-filing rule, Congress should amend § 1819(b) to make an explicit grant of federal jurisdiction to assignees of the FDIC. Although neither Congress nor the Supreme Court has rejected the time-of-filing rule, unless the Supreme Court elects to resolve this split in authority, courts can continue to apply this judge-made rule selectively. Since the time-of-filing rule has neither a statutory basis nor is it a constitutional rule, Congress may legislate a different approach.<sup>355</sup> Congress' grant of FDIC jurisdiction is based upon the FDIC's status as a federal agency. The Supreme Court's decision in *Vermont Agency of Natural Resources* suggests that a federal party's status may be assigned without running afoul of Article III.<sup>356</sup>

By extending federal jurisdiction to these asset purchasers, Congress can guarantee the benefits of certainty and efficiency provided by the time-of-filing rule to transactions between the private party purchasers and the FDIC. As assignees, private party purchasers can avoid the inconvenience and expense of defending challenges to federal court jurisdiction, and lower overall transaction costs. Such certainty will advance the FDIC's goals to recover the most value from assets of failed depository institutions, maintaining a solvent insurance fund to preserve public confidence in the banking industry.<sup>357</sup>

A legislative grant of jurisdiction to FDIC private party purchasers can also serve purposes related to federal court jurisdiction. If Congress grants private party purchasers federal jurisdiction, Congress can make certain that federal courts will exercise their discretion under the supplemental jurisdiction statute only when the requirements of § 1367(a) are met.<sup>358</sup> In addition, legislation that contains a clear statement of jurisdiction for FDIC asset purchasers would likewise deter unwanted expansion of the FDIC's federal common law.<sup>359</sup>

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354. Cf. Wright et al., *supra* note 165, § 3608 at 452. ("[I]f jurisdiction could be destroyed by a party moving to the opposing party's state after commencement, then whenever either litigant believed he might lose on the merits he could terminate the action by becoming a citizen of the other party's home state.").

355. See *supra* note 168 and accompanying text.

356. See discussion *supra* Part IV.A.2.

357. See, e.g., Galves, *Might Does Not Make Right*, *supra* note 6 at 1339-41 (discussing role of FDIC).

358. See discussion *supra* Part IV.C.

359. See discussion *supra* Part IV.A.1.

## CONCLUSION

The FDIC exercises enhanced statutory and common law powers in litigation to fulfill its role as an insurer to the deposits of national and state banks and thrifts. Whenever the FDIC is a party to a civil action, it has the advantage of federal court jurisdiction under § 1819(b)(2)(A) of FIRREA. Some federal courts faced challenges to their jurisdiction on the theory that when private parties succeeded to the FDIC as a party to ongoing litigation, they failed to satisfy requirements for federal jurisdiction independent of the FDIC.

The majority of courts follow the reasoning of the Fifth Circuit decision in *FSLIC v. Griffin*<sup>360</sup> by relying on the FDIC case law of common law *D'Oench, Duhme* and the time-of-filing rule to hold that a private party that purchases assets from the FDIC may remain in federal court despite the FDIC's departure from the litigation.<sup>361</sup> By contrast, the Third Circuit in *New Rock Asset Partners v. Preferred Entity Advancements, Inc.* took a discretionary approach by invoking the supplemental jurisdiction statute.<sup>362</sup> The majority courts properly invoke the time-of-filing rule, while the minority courts erroneously rely on § 1367(a). Instead of relying on courts to apply the time-of-filing rule, Congress should go a step further and enact legislation to confer federal court jurisdiction to these private party purchasers in order to accomplish the objectives of FIRREA and to designate clearly the scope of its jurisdictional grant.

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360. 935 F.2d 691, 696 (5th Cir. 1991).

361. See discussion *supra* Part III.A.

362. 101 F.3d 1492, 1504-11 (3d Cir. 1996).

## *Notes & Observations*

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